

Exhibit 47

1 UNITED STATES BANKRUPTCY COURT
SOUTHERN DISTRICT OF NEW YORK

2 -----x

3 In re:

4 SEARS HOLDINGS CORPORATION, et al.,
Debtor.

5
6 Chapter 11
Case No. 18-23538 (RDD)

7
8 -----x

HEARING DAY 3

9 February 7, 2019

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11 B E F O R E:

12 HON. ROBERT D. DRAIN,
UNITED STATES BANKRUPTCY JUDGE

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16 Reported by:
MARK RICHMAN, CSR, RPR, CM
17 JOB NO: 155335
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1 PROCEEDINGS

2 THE COURT: Okay, good morning.

3 In re Sears Holdings Corporation.

4 Before we begin, I just want to make
5 double sure that the court call is
6 hooked in, that the people are on it.

7 AUDIENCE MEMBER VIA PHONE: Yes,
8 your Honor, we are all set.

9 THE COURT: Okay. Because I got
10 an earlier email. Maybe that wasn't
11 the case.

12 Okay, you can go ahead, Mr.
13 Schrock.

14 MR. SCHROCK: Good morning, your
15 Honor, for the record, Ray Schrock,
16 Weil Gotshal Manges on behalf of the
17 debtors.

18 Your Honor, we are here for
19 closing arguments to finish up the
20 summary proceeding for approval of
21 substantially all of the debtors' --
22 sale of substantially all of the
23 debtors' assets to ESL and then the
24 Transformco.

25 Your Honor, I do have a few slides

1 PROCEEDINGS

2 that I'd like to walk through to
3 organize my points and my thoughts.
4 May I approach?

5 THE COURT: Sure.

6 MR. SCHROCK: Your Honor, today
7 is obviously a very important day for
8 Sears and there have been many of
9 those in the short course of this
10 case, but this is in fact may be the
11 most important day. Everything
12 depends on it.

13 The fate of Sears is going to be
14 in the court's hands. We've done
15 everything that we can to save this
16 company over the last several months.
17 And as your Honor may remember when
18 we first started this case, we put it
19 on a very fast timeline and we knew
20 that it was going to be a tremendous
21 amount of work to even get to this
22 position. But I think even by, and I
23 think I speak on behalf of all the
24 professionals and stakeholders
25 involved, I think everybody would

1 PROCEEDINGS

2 acknowledge it's frankly been even
3 more than that, it's been
4 extraordinary.

5 We very much are in support of
6 approving the sale to ESL. And the
7 primary objections that have been
8 lodged against the sale revolve
9 around whether the sale transaction
10 has been the product of an adequate
11 sale process, you know, whether or
12 not it's the highest or best
13 alternative. And we believe that the
14 evidence submitted during the summary
15 proceeding overwhelmingly
16 demonstrates that the debtors have
17 carried their burden.

18 Now, your Honor, on slide 2 we
19 also note that we have addressed a
20 few other key issues at the request
21 of the court that I'll be covering
22 this morning.

23 ESL's assuming of \$166 million of
24 accounts payable.

25 The potential overhang of warranty

1 PROCEEDINGS

2 liabilities.

3 The transition services agreement.

4 Cyrus's allowance of claims.

5 The, quote, unquote, noncredit bid
6 value for unencumbered assets.

7 Clarifying the scope of release
8 for ESL.

9 And the KCD administrative claim.

10 I'll be turning the podium over to
11 Mr. Basta following my comments to
12 cover issues related to the
13 subcommittee and the credit bid and
14 release issues.

15 Last night and this morning, we
16 filed a few documents with the court.
17 We did file a form of transition
18 services agreement. It's in
19 substantially final form. Parties
20 are still working out a few issues
21 but we believe it's very close.

22 We filed the schedules to the
23 asset purchase agreement.

24 Importantly, these schedules were
25 done at the time of signing the asset

1 PROCEEDINGS

2 purchase agreement and that schedule
3 contains, among other things, a
4 schedule 1 G that demonstrates that
5 the \$166 million of accounts payable
6 was in fact agreed to be assumed by
7 ESL.

8 Just to put it out there, judge,
9 this is an important issue. We have
10 not come to terms with ESL on that
11 particular point. The debtors are
12 prepared to close on the contract as
13 written. But we will be asking the
14 court for the court's guidance.
15 We're not going to engage in
16 litigation post closing. If ESL is
17 prepared to close on the agreement as
18 written, take the 166, we have a
19 deal. If they're not, then we don't
20 have a deal. And I think that's
21 where the parties are at the moment.
22 But I do have copies of the schedules
23 if you'd like.

24 THE COURT: I was going to ask
25 you for that schedule in particular.

PROCEEDINGS

MR. SCHROCK: Certainly.

THE COURT: 1.1 G or 1 G?

MR. SCHROCK: Yes, your Honor.

THE COURT: Other payables.

MR. SCHROCK: So, your Honor, as
it does demonstrate on schedule 1 G,
1.1 G, which is defined as other
payables --

THE COURT: It just says 166
million. I assume accounts payable.

MR. SCHROCK: Yes.

THE COURT: Okay. You put it
about as broad as you can get.

MR. SCHROCK: That's about as far
as we could get, your Honor. And
taking it a little bit out of order,
but on the KCD administrative claim,
I do have an important announcement
for the court and parties in
interest.

I am very pleased to report that
last evening the debtors
restructuring committee agreed to a
settlement term sheet with the PBGC.

1 PROCEEDINGS

2 That settlement results in a number
3 of things and a number of benefits
4 for these estates, but it doesn't
5 just resolve their objection to the
6 sale. It also resolves their claims
7 in these cases.

8 Your Honor, I do have a copy of
9 the settlement term sheet that I'll
10 be prepared to walk through and hand
11 it up to you and we have copies for
12 parties in interest.

13 THE COURT: Okay.

14 MR. SCHROCK: So, your Honor,
15 this settlement proposal which really
16 is phenomenal, we have come to an
17 arrangement where the PBGC will
18 withdraw their objection to the ESL
19 sale. This agreement is not
20 contingent upon closing of the ESL
21 transaction. But we have agreed and
22 the debtors have agreed importantly
23 that, to the consensual termination
24 of the Sears pension plan and K-Mart
25 pension plan effective as of January

PROCEEDINGS

31, 2019.

Now importantly this is just an agreement to the debtors. This does not affect the obligations or the rights and cannot be used as a sword against nondebtors.

There's going to be an agreement on a claim that, a general unsecured claim that will be held against all debtors because there is a joint and several claim. It's been lowered from the asserted amount of roughly \$1.7 billion to \$800 million.

The termination premium is not going to -- the debtor is not going to be liable for that. And importantly, the PBGC would be willing to support a Chapter, it will support a Chapter 11 plan, subject to approval of disclosure statement, both the claims in favor of a plan.

The PBGC which holds -- which has a director at KCD will also take steps with the debtors to ensure that

1 PROCEEDINGS

2 any claims of KCD against the debtors
3 are waived in total.

4 So importantly, the \$111 million
5 claim that's been talked about and
6 that I think the committee's
7 witnesses, the debtors and myself
8 have said, listen, this is an
9 administrative claim, that claim --

10 THE COURT: Potentially one.

11 MR. SCHROCK: Potentially one, is
12 in fact resolved.

13 Because of the steps that the PBGC
14 has taken in conjunction with the
15 sale, because of the steps they've
16 taken to assist us with the, all of
17 the issues with the administrative,
18 purported administrative claim, the
19 substantial reduction in their
20 allowed claim as a general unsecured
21 claim for 1.7 down to roughly \$800
22 million, we are agreeing that under
23 the terms of a plan that they would
24 have a priority right to \$80 million
25 of net proceeds in litigation

1 PROCEEDINGS

2 actions. There's also a release.

3 And this is subject to us documenting
4 this and moving forward for approval
5 on settlement.

6 Now importantly that settlement is
7 not up for approval today. But I
8 think for purposes of this hearing,
9 your Honor, what matters is the PBGC
10 is withdrawing its objection and the
11 debtors we believe -- we have a path
12 forward to resolve the KCD
13 administrative claim. Nothing's
14 guaranteed, and nothing's guaranteed
15 in this case on administrative
16 solvency in an ESL sale, nor is it
17 guaranteed certainly in a winddown.
18 There's heavy risk, in our view,
19 around the winddown. And we will
20 talk more about this.

21 THE COURT: So you'll be seeking
22 approval of this settlement, the
23 aspects that aren't that go into
24 effect immediately?

25 MR. SCHROCK: That's correct.

1 PROCEEDINGS

2 THE COURT: I'm assuming
3 reasonably promptly or maybe it will
4 be in the context of approval of the
5 plan, maybe it will be separate.

6 MR. SCHROCK: I expect, your
7 Honor, we're going to document a plan
8 and likely a restructuring and
9 support agreement promptly with court
10 approval. We are also going to sit
11 down with the committee on the terms
12 of a plan. So we haven't worked out
13 precisely what's going to be in the
14 context of the plan or separate, but
15 we will be moving forward promptly.

16 THE COURT: I know counsel for
17 the PBGC has participated. Is that a
18 fair summary of the settlement? I
19 mean I have the signed term sheet.

20 MR. RADER: Good afternoon, your
21 Honor. For the record, Brian Rader
22 on behalf of PBGC. Everything that
23 Mr. Schrock says is consistent with
24 the term sheet. And one obligation
25 under the term sheet is to formally

1 PROCEEDINGS

2 withdraw our objection to the sale,
3 and I'd like to do that on the record
4 right now.

5 THE COURT: Okay, very well.
6 Thank you.

7 MR. RADER: Thank you, your
8 Honor.

9 MR. SCHROCK: Your Honor, moving
10 on from the PBGC settlement. We
11 think the evidence in this matter is
12 very much largely uncontroverted.

13 THE COURT: I'm sorry. Can I go
14 back to your slide.

15 MR. SCHROCK: Yes, which one?

16 THE COURT: You mentioned the
17 transition services agreement and I
18 haven't had a chance to review that
19 yet. Is it essentially neutral to
20 the debtors? Are the debtors
21 performing obligations under it that
22 they can't perform because they don't
23 have the money to do so, or
24 alternatively are they relying on ESL
25 to perform obligations that they

PROCEEDINGS

don't have the money to do so?

MR. SCHROCK: Your Honor, I think it's fair to say, like most transition services agreement, it's a framework for the parties to work together over the near term. And given the pace at which this is closing, there are some things that ESL needs from the debtor, such as, you know, transform Postco license to conduct business and they're going to need to use the debtors' licenses. They're leasing the debtors' employees. We're getting access to books and records to finish the conduct of the case. There is agreement from the debtors for some cash payments over the next 60 days for the use of -- for the use of basically facilities, conducting GOBs, liquidating inventory.

THE COURT: By the debtors.

MR. SCHROCK: By the debtors.

THE COURT: In respect to

1 PROCEEDINGS

2 pursuing assets.

3 MR. SCHROCK: Yes, over the next
4 60 days. Now we can agree to extend
5 that 60 day time frame. We can come
6 to an agreement, as is common.

7 I don't -- one thing is for
8 certain, your Honor. Like every
9 other transition services agreement,
10 I'm very confident that the parties
11 are going to have to supplement it
12 because as you know, if we can, are
13 fortunate enough to close the
14 transaction tomorrow, parties are
15 going to need to be able to work
16 together.

17 THE COURT: I understand that. I
18 just want to make sure that it's
19 essentially neutral that the benefits
20 the debtor is getting -- the debtors
21 are getting out of it are no less
22 than what they're paying for it and
23 vice-versa.

24 MR. SCHROCK: That is very
25 much --

1 PROCEEDINGS

2 THE COURT: And what ESL is
3 getting out of it are going to be
4 paid by ESL.

5 MR. SCHROCK: That is very much
6 the intent, your Honor. There are
7 modest cash payments from the company
8 coming out of that. But when you go
9 through all of the back and forth --

10 THE COURT: Is the company
11 providing services to ESL?

12 MR. SCHROCK: Yes.

13 THE COURT: Is it being
14 compensated for that?

15 MR. SCHROCK: It's all being
16 taken into account in terms of the
17 back and forth in terms of who is
18 providing what services. At the end
19 of the day, there's a net payment
20 coming from the debtors. But we
21 believe that it's a fair compromise
22 in light of what's being required
23 from all the parties on each side.
24 But primarily we're going to need
25 access to Transformco assets.

1 PROCEEDINGS

2 THE COURT: As far as the
3 services the debtors are providing,
4 will they have the resources to
5 provide those services?

6 MR. SCHROCK: Yes, your Honor.

7 THE COURT: Will they pay for it
8 if they don't?

9 MR. SCHROCK: Yes, your Honor.

10 THE COURT: Is that ESL's
11 understanding too?

12 MR. BROMLEY: Your Honor, James
13 Bromley, Cleary Gottlieb on behalf of
14 ESL. The answer is yes. The TSA is
15 structured in a way that the debtors
16 would be paying \$1.25 million a month
17 during this period of time subject to
18 extension to ESL for a vast host of
19 services, the cost of which is much
20 in excess of 1.25.

21 For the services that the debtors
22 are providing back to ESL, there will
23 be a payment from ESL of 250,000 a
24 month. So the net is a million
25 dollars a month during that period of

1 PROCEEDINGS

2 time, 60 days subject to extension.

3 THE COURT: And the primary
4 services are, in essence, being able
5 to do GOB sales? I mean is that
6 keeping the access to the properties?

7 MR. BROMLEY: There's a variety
8 of things. That's one of them, your
9 Honor. But upon closing, assuming
10 that the sale closes, nearly all of
11 the debtors' operations will be
12 transferred to the buyer and the
13 debtor needs some of those services
14 back in order to continue its
15 operations in winddown. So in that
16 sense ESL, or the Newco will be
17 providing those services back to the
18 estate.

19 And in terms of the cost neutral
20 element of it, the cost of providing
21 those services by Newco is far in
22 excess of the net million dollars
23 that's going to be paid by the
24 debtor.

25 THE COURT: Okay.

1 PROCEEDINGS

2 MR. SCHROCK: And I mean from the
3 estate's perspective, judge, the
4 primary thing that we believe we're
5 getting, access to books and records,
6 we don't think that's something --

7 THE COURT: I mean that's in the
8 contract.

9 MR. SCHROCK: That's in the
10 contract. It's not really a big
11 deal. We need access to finish GOBs,
12 to bring those assets into the
13 estates. They need from us
14 licensing. That's the real trade
15 here over the next 60 days. But when
16 we did the math --

17 THE COURT: And then taking some
18 of your, or all of your people
19 primarily or almost all of them.

20 MR. SCHROCK: Almost all the
21 people.

22 THE COURT: So some of them will
23 continue to provide the services you
24 need related to the winddown for the
25 rest of the case.

1 PROCEEDINGS

2 MR. SCHROCK: Yes, your Honor.

3 Importantly, we are agreeing to,
4 we're leasing employees in fact to,
5 under the transition services
6 agreement, to Transformco over the
7 near term. So those employees are
8 still going to be technically the
9 debtors' employees for a period of
10 time until they get their systems up
11 and running.

12 THE COURT: Okay. We have some
13 other things on here. Are you going
14 to get to those later or do you want
15 to cover them now? The warranties,
16 the Cyrus release.

17 MR. SCHROCK: Your Honor, we can
18 take those now. The potential
19 overhang on warranties, if your Honor
20 were to turn to slide 27. There's a
21 provision in the agreement that
22 pending the transfer of the KCD notes
23 --

24 THE COURT: I'm sorry, so this
25 isn't anything new?

1 PROCEEDINGS

2 MR. SCHROCK: No.

3 THE COURT: I just want you to
4 summarize anything new. I'm sorry.

5 MR. SCHROCK: If that's a
6 clarification under the agreement
7 that's already handled.

8 Going through this list --

9 THE COURT: If there's anything
10 new on here as opposed to explaining
11 as part of your organize argument,
12 you should let me know.

13 MR. SCHROCK: The scope of the
14 release is the only other thing that
15 I think Mr. Basta will address.

16 THE COURT: And related to that
17 is Cyrus, I guess.

18 MR. SCHROCK: That's right, but
19 Cyrus I will handle in argument as
20 will Mr. Basta but it's literally
21 nothing changed.

22 THE COURT: Okay.

23 MR. SCHROCK: Your Honor, moving
24 forward on slide 3, the evidence in
25 this matter is largely uncontroverted

1 PROCEEDINGS

2 in favor of a number of solutions,
3 including that the sale transaction
4 is subject to business judgment
5 standard and that we meet the
6 standard as a valid exercise of the
7 debtors' business judgment.

8 The sale process is thorough,
9 competitive, and a highly public
10 process carried out in compliance
11 with the court's approved global
12 bidding procedures.

13 The sale transaction is superior
14 to the winddown alternative and
15 Transformco has provided adequate
16 assurance of future performance.

17 Your Honor, the legal standard is
18 set out in 363 (B) (1) that the
19 trustee, after notice and a hearing,
20 may use, sell, or lease, other than
21 in the ordinary course of business,
22 property of the estate.

23 Courts in this circuit and others,
24 in applying this section, have
25 required that the sale of the

1 PROCEEDINGS

2 debtor's assets must be based on the
3 sound business judgment of the
4 debtor.

5 Now where the transaction is
6 negotiated or supervised by an
7 independent fiduciary, such as a
8 restructuring committee, the business
9 judgment standard we believe
10 undoubtedly continues to apply.

11 This is an unusual auction, judge,
12 in that in every other auction
13 certainly that I've been involved in,
14 you are comparing two live bidders,
15 one bid being, you know, could be a
16 going concern bid and another bid, at
17 least if there's a liquidation
18 alternative, there is at least, you
19 know, a liquidator that's really
20 putting up cash, that's providing
21 real value.

22 Here the company only had one
23 qualified bid, okay, for the auction,
24 for going concern sale. We were
25 comparing it to a winddown

1 PROCEEDINGS

2 alternative run by the debtors, okay.

3 And we took that obligation very
4 seriously nevertheless. But I do
5 think it's worth noting that the only
6 qualified bid was for -- was from ESL
7 and Transformco.

8 THE COURT: Can I explore that a
9 little bit.

10 MR. SCHROCK: Sure.

11 THE COURT: There really was not
12 a whole lot in the record on this.
13 But the prior hearings leading up to
14 the auction referenced the debtors
15 soliciting I guess it's bulk bids
16 from liquidators.

17 MR. SCHROCK: Yes.

18 THE COURT: And the debtors
19 announced their conclusion that their
20 retained liquidator, Abicus, actually
21 had the best of that lot of that
22 group. Abicus, when you refer to
23 Abicus being the best of that group,
24 is that just based on the terms of
25 Abicus's retention?

1 PROCEEDINGS

2 MR. SCHROCK: It is, your Honor,
3 based on the terms of Abicus's
4 retention. And when we were looking
5 at so-called equity bids from
6 liquidators where they were actually
7 going to be purchasing the assets,
8 the recoveries that could be had on
9 the company's assets was simply
10 superior under a company run GOB.
11 And I don't really think that issue
12 is in controversy by any of the
13 stakeholders in this case.

14 THE COURT: Well certainly no one
15 has raised the argument that any of
16 the liquidators made a higher or
17 better bid.

18 Were those proposals including the
19 Abicus one, did they include Abicus
20 running anything more than GOB sales,
21 i.e., did they assume that the
22 company would be -- the debtors would
23 be marketing the real estate assets
24 separately from the liquidators?

25 MR. SCHROCK: Your Honor, there

1 PROCEEDINGS

2 are various permutations of those
3 bids. And the debtors actually ran
4 an informal auction during the first
5 week of January among the liquidators
6 in the event that we were going to go
7 the GOB route.

8 The results of that auction --

9 THE COURT: We announced that.

10 MR. SCHROCK: The result of that
11 was that Abicus was a higher or
12 better bid. But we don't have, you
13 know, deposits, qualified bids from
14 liquidators. And I think that how
15 the parties and the committee and the
16 debtors certainly agreed that the
17 recovery under it was an Abicus and
18 we also supplemented with SB 360,
19 Schottenstein, a Schottenstein run
20 venture, to provide additional
21 capacity, that those two parties
22 running the GOBs with the debtors
23 would provide the highest or
24 recoveries and that's what we were
25 comparing in the context of the

1 PROCEEDINGS

2 auction and the winddown.

3 THE COURT: I guess my question
4 is, the Abicus terms, were those set
5 forth in the retention? You didn't
6 change those?

7 MR. SCHROCK: Yes, your Honor.

8 THE COURT: Except they added
9 SB360 which sounds like a product
10 that Sears would be selling as
11 opposed to buying.

12 MR. SCHROCK: Yes, your Honor.
13 The answer is yes. It's very modest.

14 THE COURT: So can I interrupt
15 you. As I remember that retention,
16 they didn't take on the
17 responsibility to market real estate.
18 It was really straight GOB.

19 MR. SCHROCK: That's correct.

20 THE COURT: So --

21 MR. SCHROCK: That's right.

22 THE COURT: So when you compared
23 the various ESL proposals including
24 the one that was ultimately accepted
25 to a liquidation alternative, it was

1 PROCEEDINGS

2 a combination of Abicus GOB sales and
3 the debtors marketing real estate.

4 MR. SCHROCK: That's correct,
5 your Honor. So we used a combination
6 of, as provided in the testimony from
7 Mr. Meghji as well as Mr. Welch, a
8 combination of appraisals that we had
9 conducted for assets as well as
10 indications of interest received and
11 comparing how we received them.

12 THE COURT: There's some
13 miscellaneous assets in potential
14 litigation claims, but it was
15 primarily GOB and real estate. And
16 you're still doing the GOB.

17 MR. SCHROCK: We are still doing
18 the GOB.

19 THE COURT: So it comes down to
20 the real estate.

21 MR. SCHROCK: That is it. I
22 think when you really looked at the
23 differences between the committee's
24 assumptions and the debtors'
25 assumptions around the winddown, it

1 PROCEEDINGS

2 really did in our view come down to
3 the real estate. You had, you know,
4 from the one perspective the debtors,
5 the debtors' valuations that are in
6 the record. They are uncontested.
7 And during Mr. Greenspan's live
8 testimony, he retracted his two
9 important criticisms of the Welch
10 declaration and lessened his
11 valuation by 50 to \$90 million.

12 I note that Mr. Greenspan also was
13 assuming what I can only say is just
14 a process that's not bound in reality
15 or 365 (B) (4) bankruptcy code that
16 you can liquidate leases over the
17 course of 20 to 24 months and saying
18 you're going to assume those leases
19 and put them in a trust.

20 I think this does not recognize
21 what the legal restrictions are and
22 the assumption and assignment under
23 the bankruptcy code.

24 And as Mr. Welch further
25 explained, the discounts applied by

1 PROCEEDINGS

2 M-III related to the real estate were
3 reasonable because they accounted for
4 an unprecedented expedited bulk sale
5 of big box properties from a
6 distressed seller.

7 In fact, Mr. Greenspan himself
8 testified that sale of the properties
9 of the magnitude contemplated by the
10 debtors was unprecedented.

11 The liquidation winddown analysis
12 reasonably values the real estate.
13 We think the Toys experience does
14 support our valuation. But I do
15 believe that overall when you look at
16 the appraisals and the rigor through
17 which the debtors put all of these
18 properties through that test,
19 demonstrates that the ESL value, and
20 we'll talk more about it, was in fact
21 much greater for all of the creditors
22 at large.

23 Your Honor, slide 5 we talk a
24 little bit about the marketing
25 process and I think it's really worth

1 PROCEEDINGS

2 noting that Mr. Aebersold's testimony
3 in this matter is largely
4 uncontroverted.

5 Their initial phase was designed
6 to provide a large number of
7 potential purchasers with
8 information. We engaged with over
9 250 potential investors, 125 under
10 NDA.

11 It was extraordinary. The debtors
12 and their advisors responded to
13 several hundred diligence questions,
14 held over 40 formal diligence calls
15 and in-person meetings.

16 In multiple formal meetings and
17 numerous other informal discussions
18 with the UCC, the debtors outlined
19 their marketing strategy, shared the
20 identity of prospective bidders,
21 facilitated in-person meetings with
22 management and gave the opportunity
23 to review and comment on proposed
24 purchase agreements for prospective
25 bidders.

1 PROCEEDINGS

2 Now the UCC had the opportunity to
3 ask Mr. Aebersold about the sales
4 process but they really didn't ask a
5 single question, I believe, about
6 that process. And they cannot now
7 challenge that process with the
8 evidence closed.

9 THE COURT: I think you're about
10 to go to a different point. Turning
11 back to the real estate, the debtors'
12 committee asserts that the debtors
13 did not run a real estate auction per
14 se. They instead ran an auction
15 where they posited their assumed
16 values for the real estate as a
17 counter to the one going concern
18 proposal that was qualified which was
19 the ESL proposal. And they suggest
20 that if you run a parallel real
21 estate auction, that instead of the
22 relatively modest number of
23 expressions of interest, or
24 indications of interest, you would
25 have gotten a much bigger number.

1 PROCEEDINGS

2 And I guess my question is why
3 wasn't that done and could it have
4 been done?

5 MR. SCHROCK: Yes, your Honor, I
6 think with due respect to my friends
7 on the committee, I think that they
8 have a selective memory on this
9 issue. Because when we first
10 undertook the global sale process and
11 had it approved, we were very open
12 with the committee, we were very open
13 with all parties we have to do what's
14 within the realm of the possible. So
15 we set up the case so we had a chance
16 to run a process, an expedited
17 process on a going concern sale.

18 We told parties during December
19 that if they wanted to put in
20 indications of interest for the
21 debtors to consider, that we would
22 certainly -- that we would consider
23 them. But as we told the committee,
24 we were going to be relying, you
25 know, also on nonbinding indications

1 PROCEEDINGS

2 of interest which were due by the
3 28th and the debtors' appraisals in
4 comparing the market value.

5 We have plan exclusivity. We
6 think that the record -- you don't
7 have to run a full real estate
8 process. And I think frankly
9 marketing, you know, 500 properties
10 in this amount of time, when you talk
11 about what's within the realm of the
12 possible, your Honor, in our
13 judgment, and we have a lot of people
14 working on this matter, that was not
15 possible to run a full real estate
16 process simultaneously with running
17 the going concern process.

18 But we did test the market. The
19 evidence is uncontroverted on exactly
20 what the debtors did do. I think
21 that if we were in contact with the
22 committee during this time, we had
23 global asset sale procedure process
24 that we followed to the letter with
25 the court.

1 PROCEEDINGS

2 And, your Honor, during that
3 process we found that there was one,
4 effectively one qualified bid. But
5 those nonbinding indications of
6 interest, we didn't have a lot of
7 deposits, we didn't have a lot of
8 serious offers. It was our
9 contemplation that if we weren't able
10 to have a going concern sale, because
11 we looked at the values and we made
12 we thought generous assumptions
13 around the real estate that if we
14 couldn't really substantially reduce
15 claims, have a going concern
16 opportunity, either in whole or in
17 part by selling divisions or selling
18 the whole business, that then in fact
19 we would have to pivot during the
20 winddown process to a full real
21 estate liquidation process.

22 THE COURT: Okay. So I want to
23 make sure I understand this. To
24 summarize, and I guess this is
25 consistent with both Mr. Welch and

1 PROCEEDINGS

2 Mr. Greenspan's testimony, you're
3 saying you could not run an actual
4 real estate sale process in the
5 roughly month and a half, two months
6 that you had. In fact, the minimum
7 time for such a process would be four
8 months and according to Mr. Greenspan
9 it would have to be over a year.

10 MR. SCHROCK: That's right, your
11 Honor.

12 THE COURT: So you did instead,
13 recognizing that time was valuable
14 here and recognizing the risks of
15 going with just a going concern
16 process without a some reality check
17 beyond appraisals, which is, real
18 estate is not like valuing tech
19 assets, real estate's real estate,
20 you can do a pretty good valuation of
21 real estate.

22 You did indicate strongly to those
23 who might believe that a liquidation
24 process with the sale of the real
25 estate would be better, to actually

PROCEEDINGS

put their best foot forward and make at least indications of interest. Which is frankly what I said too during the hearing on the approval of the sale procedures looking right at counsel for various potential buyers of real estate and the creditors' committee, i.e., if you really believe this, put your best foot forward and make a proposal.

Okay.

MR. SCHROCK: And, your Honor, building on that, on slide 6 we do note that, and it's really worth emphasizing, this is a process that was conducted pursuant to the court approved global bidding procedures. We have followed those procedures throughout the case. The report is uncontroverted on that piece.

We have determined what is the successful bid consistent with the global bidding procedures, which qualified bids constitute the highest

1 PROCEEDINGS

2 or best qualified bids. And pursuant
3 to the auction rules, that was
4 determined in the business judgment
5 of the debtors.

6 We also had an independent chief
7 restructuring officer that the court
8 heard from, Mr. Meghji, an
9 independent restructuring committee.
10 You heard from both of the
11 subcommittee members. They were all
12 very active during this process.

13 And, your Honor, on slide 7 we do
14 note that I think the record is fully
15 uncontroverted that restructuring
16 committee here is independent. And
17 having certainly lived through this,
18 your Honor, I can vouch that it very
19 much is, that there's a couple of
20 anecdotes here just in regard to
21 that, that the testimony of Mr. Carr
22 as well as Mr. Transier is that they
23 did not have any association or
24 interactions with Mr. Lampert prior
25 to joining the board. We put

1 PROCEEDINGS

2 together an independent restructuring
3 committee. I think ESL knew that if
4 they, given their position within the
5 capital structure, that this is going
6 to be necessary. But there's no
7 personal or business relationship
8 either prior to or since that time
9 with either of the subcommittee
10 members.

11 This independent restructuring
12 committee negotiated, reviewed, they
13 approved the sale transaction. They
14 were specifically delegated with the
15 authority to negotiate and approve
16 the ESL transaction.

17 And the record in these
18 proceedings is that the restructuring
19 committee was actively involved. No
20 less than 58 times prior to the
21 proposed ESL transaction being
22 approved did the restructuring
23 committee meet since being formed in
24 October 2018. And these were not
25 short meetings. These were lengthy,

1 PROCEEDINGS

2 involved meetings, numerous in-person
3 meetings. The directors, the
4 professionals, everyone took their
5 job extremely seriously and their
6 responsibilities to these estates.

7 Mr. Aebersold further testified
8 that consistent with his experience,
9 that the sale process was extensive.
10 We gave you some anecdotes to that
11 earlier, and that to his knowledge
12 and based upon his observations and
13 experience the auction was conducted
14 in good faith and the sale process
15 provided a fair and reasonable
16 opportunity to purchase components of
17 substantially all the debtors' assets
18 and operations.

19 That evidence is uncontroverted.

20 And further, your Honor, in
21 talking about how independent this
22 committee was, the committee formally
23 voted to reject separate bids by ESL
24 on at least two occasions. This was
25 in my experience very unusual. I

1 PROCEEDINGS

2 mean it's a very tight transaction I
3 think for ESL as well as the estate.
4 But this is not something where
5 anyone was pandering to anyone at ESL
6 and there's certainly no record to
7 support that.

8 We think the sound business
9 justifications here are consistent
10 with case law in the Second Circuit.

11 We point to Chrysler, among
12 others. But there's in announcing
13 and looking at what types of
14 consideration that the court can
15 consider, I think it's worth
16 reiterating just looking at what ESL
17 and Transformco are providing.
18 They're committing approximately \$5.2
19 billion in the form of cash and
20 noncash consideration, including a
21 cash payment of approximately \$885
22 million. There's a credit bid
23 pursuant to 363 (K) of the bankruptcy
24 code of secured debt facilities
25 totalling approximately 1.3 billion.

1 PROCEEDINGS

2 There's the assumption of \$621
3 million of senior debt, including
4 \$350 million of the amounts owed
5 under the Junior DIP facility and
6 \$271 million of the standalone LC
7 facility.

8 Those are all senior claims to
9 senior unsecured creditors.

10 There's further the assumption of
11 certain of the other debtors
12 liabilities in the total amount of
13 approximately \$1.3 billion, including
14 liabilities for warranties and
15 protection agreements or other
16 service contracts, certain customer
17 credits to existing customer loyalty
18 programs, the Shop Your Way program,
19 all cure costs are being assumed by
20 ESL.

21 There's up to \$43 million of
22 certain severance reimbursement
23 obligations. There's up to \$139
24 million of 503(b)(9) claims. And
25 just to hit that for your Honor,

1 PROCEEDINGS

2 you've asked what's the mechanism to
3 do that.

4 The debtors are obligated to
5 reconcile those claims and there's
6 not an independent right of claimants
7 to go after ESL. But ELS is
8 obligated to the estate to pay those
9 503(b)(9) claims upon the earlier of
10 120 days and confirmation of a plan.

11 Our experience, and we do have an
12 \$80 million winddown budget that's
13 built into how we intend to finish
14 these cases, it's our expectation
15 that we will do the reconciliation,
16 finish the reconciliation around the
17 503(b)(9) claims.

18 We don't expect a lot of costly
19 litigation certainly around the
20 503(b)(9) claims, but those claims
21 are going to be paid by ESL at
22 confirmation of the plan.

23 THE COURT: The 89 million
24 winddown budget, is that included in
25 the projections that Mr. Meghji went

1 PROCEEDINGS

2 through?

3 MR. SCHROCK: Yes.

4 THE COURT: On this insolvency
5 analysis?

6 MR. SCHROCK: It is, your Honor.

7 THE COURT: So the debtors will
8 be reconciling those claims,
9 potentially objecting to them. Many
10 of those claimants I would assume
11 would have an ongoing relationship
12 with, if I approve the sale, the
13 buyer.

14 MR. SCHROCK: That's right.

15 THE COURT: Is it contemplated
16 there will be some interactions since
17 the buyer is liable for them, how to
18 resolve those claims?

19 MR. SCHROCK: There's going to be
20 a lot of interactions, your Honor. I
21 think one thing that ELS and the
22 debtors do recognize, if the sale is
23 approved and we close tomorrow, it's
24 still all the same people that are
25 really doing this work at the

1 PROCEEDINGS

2 company. And we're going to be
3 working together. And the TSA, the
4 transition services agreement
5 certainly contemplates that we're
6 going to be cooperating, working in
7 good faith to finish the
8 administration of the cases.

9 ESL is heavily incentivized.
10 They're still a very large claimant,
11 as is Cyrus, in these estates to have
12 these cases administered efficiently.

13 And I don't want that to be lost
14 on the court. They still have claims
15 in these cases. They still have
16 every incentive to cooperate. They
17 still have every incentive to work
18 with the company to minimize the
19 costs associated with the
20 administration of the estate.

21 But when I look at what are the
22 noncredit bid items that are really
23 being provided for unencumbered
24 assets and I'm looking at slide 13
25 and 14, all of these liabilities,

1 PROCEEDINGS

2 it's just the one credit bid item but
3 paying off senior debt before
4 unsecureds are going to be paid, the
5 assumption of all of these
6 liabilities, the cure costs, these
7 are all things that we negotiated for
8 in order to ensure that -- you know
9 these are unsecured claims that are
10 getting paid. Property taxes,
11 environmental liabilities, the
12 mechanic's liens are senior secured
13 claims.

14 So they are all either senior or
15 parity with general unsecured
16 creditors, but there's a lot of -- we
17 focused on the exit facility but
18 there's cash being paid for these
19 senior claims.

20 And when we look at Cyrus, your
21 Honor, Cyrus is rolling the entire
22 Junior DIP facility. It went out and
23 purchased the rest of it, repurchased
24 that claim. They put it and its part
25 of the asset financing for this

1 PROCEEDINGS

2 company upon emergence.

3 And I think that if you didn't
4 give them something in terms of an
5 allowance of claim, we would be
6 defeating the very purpose of doing
7 this transaction because the
8 committee could simply, or any party
9 could frankly just go challenge
10 Cyrus's claims for
11 recharacterization.

12 So although ESL can technically
13 drag other parties within their
14 facility along for a credit bid, if
15 you think about it, if they didn't
16 have the ability to credit bid, if
17 that wasn't part of the release for
18 Cyrus, you could move to
19 recharacterize, go after those Cyrus
20 claims and undo the very transaction
21 we're trying to accomplish here.

22 So we have to have certainty of
23 closing. And we thought that, your
24 Honor, they're still liable. The
25 scope of the release is just related

1 PROCEEDINGS

2 to the credit bid, okay. It's not --
3 and the allowance of their claims.

4 It's not any broader than that.
5 And for the transaction even to work,
6 for the transaction to close we had
7 to provide that. But we did take
8 that into account in looking at, you
9 know, Cyrus is a very substantial
10 claim holder. They've come into this
11 process. Nothing is going to affect
12 the investigation and the ongoing
13 claims that the estate has, other
14 than just related to that credit bid.
15 And we think at the end of the day
16 that was a very fair compromise as
17 part of this transaction.

18 THE COURT: So it would pertain,
19 for example, if it turned out, I have
20 no view on whether it will turn out
21 this way, but if it turned out that
22 the sale of the MTN notes --

23 MR. SCHROCK: Right, nothing --

24 THE COURT: -- was somehow
25 collusive, that that's not being

PROCEEDINGS

released.

MR. SCHROCK: That is not being released, avoidance action is not being released. Only thing, it's consistent with the scope of the ESL release and I think Mr. Basta will be hitting some of those points.

Your Honor, on slide 15, just to point it out, when you look at the benefits of the -- the risks of the winddown --

THE COURT: I'm sorry, before you get to that slide. So you were talking about the amount and consideration in addition to the credit bid.

MR. SCHROCK: Yes.

THE COURT: When you look at a -- this is a question for both sides. When you look at the presumed value or assumed value of the unencumbered assets, the assets that, in other words, that ESL/Cyrus don't have a lien on, how do they match up?

1 PROCEEDINGS

2 Because you can't credit bid on
3 something you don't have a lien on,
4 so that means you have to pay
5 something else for it.

6 MR. SCHROCK: Yes. Of course,
7 your Honor. So a couple of things
8 here. I mean of course when we're
9 comparing it to the alternative in
10 the winddown we don't have the luxury
11 of just assuming you just get all of
12 those amounts of course. We have to
13 look at them in the context of the
14 winddown analysis and the continued
15 burn that would occur and costs that
16 would be incurred that are senior to
17 those unsecured claims.

18 But, you know, to answer your
19 question directly, I think it's fair,
20 your Honor. The credit bid is \$1.3
21 billion. Everything else here, your
22 Honor, payment of claims that are
23 senior to unsecured creditors, okay,
24 those all have to be paid regardless
25 of whether or not we're here, we're

1 PROCEEDINGS

2 at a winddown.

3 THE COURT: Just to cut through
4 it to do the math, you're saying
5 basically if the total value of the
6 ESL deal is \$5.2 billion, if you
7 subtract a billion-three from that.

8 MR. SCHROCK: That's right.

9 THE COURT: There's 3.9 billion
10 of value provided for the
11 unencumbered assets.

12 MR. SCHROCK: That's right.

13 THE COURT: Has anyone placed a
14 value on unencumbered assets anywhere
15 close to 3.9 billion?

16 MR. SCHROCK: No, your Honor.

17 THE COURT: Okay.

18 MR. SCHROCK: Your Honor, we
19 think it's unquestionable that the
20 benefits of a sale transaction
21 outweigh --

22 THE COURT: I'm sorry. You were
23 going through the sale process at
24 what people refer to as the auction.
25 One of the provisions of the sale

1 PROCEEDINGS

2 procedures order, all of which are
3 waivable in the exercise of judicial
4 duties, is to require qualified
5 bidders to provide an allocation of
6 what -- what assets they're paying
7 what for. It's uncontroverted that
8 ESL did not do that.

9 I have traditionally viewed --

10 MR. SCHROCK: We waived it, your
11 Honor.

12 THE COURT: You waived that
13 condition.

14 MR. SCHROCK: We did.

15 THE COURT: I have viewed that
16 condition, which appears in sale
17 orders, generally as serving the
18 purpose of letting a seller, the
19 debtor and its constituents, value a
20 global proposal as against piecemeal
21 proposals so that you can slice and
22 dice the auction to see whether some
23 combination of bids will equal a
24 global bid or a reduced global bid.

25 It also though does have the

1 PROCEEDINGS

2 benefit of giving you the debtors --
3 giving you the buyers' viewpoint of
4 what the -- the buyers credit bid of
5 what the unencumbered assets are.

6 But maybe you can just tell me,
7 why did you waive it here?

8 MR. SCHROCK: Your Honor, at the
9 end of the day we didn't have
10 qualified bids for even sections of
11 the business. And when we looked at
12 this in total and given that the
13 structure of the auction was going to
14 be a comparison of the debtors
15 looking at a going concern versus a
16 winddown, while we did have some
17 indications from ESL around
18 allocations and a view we had to
19 take, and I think it's fair to take
20 -- we took a global view as to what
21 consideration was being provided to
22 the company. And we understood that
23 the entire business would have to be
24 valued as a whole.

25 But given that we didn't have any

1 PROCEEDINGS

2 particular bids or qualified bids for
3 particular divisions, that wasn't as
4 much of a concern for the company.

5 THE COURT: Okay.

6 MR. SCHROCK: So the benefits of
7 the sale transaction really do
8 significantly outweigh an orderly
9 winddown.

10 Your Honor, I know there's been
11 press around the debtors' severance
12 obligations and what we were doing.
13 I do want to make clear for the
14 record that under either scenario the
15 debtors were honoring severance
16 obligations. Those claims are
17 administrative claims in these cases
18 under governing Second Circuit
19 precedent.

20 We deliberately made sure that and
21 it was one of the primary purposes
22 around having the winddown, to make
23 sure we could pay severance claims.

24 But we are entitled to take into
25 account in turning the highest or

PROCEEDINGS

best offer not just the economic point. And people make light of it. But there's 45,000 people out there that are working for this company. And it matters. These people will have jobs. As a going concern we've got uncontroverted testimony from Mr. Kamalani about the steps that they're taking with this business plan. This business plan is being financed by major commercial banks.

They and we are true believers in a going concern for sales -- for Sears, rather.

In a winddown we're going to lose all those jobs. With the exception of probably a few stores and perhaps in Guam, Puerto Rico where there are some highly profitable operations, we would have to GOB them. And we see certain businesses could be possibly sold in divisions in parts. But, your Honor, this truly is like many retailers, it's a melting ice cube

1 PROCEEDINGS

2 and the timing is so urgent. We saw
3 that even with the Services.Com
4 purchase of Parts Direct which ended
5 up with them not closing. We're now
6 going to end up having to argue with
7 them around the return of the
8 deposit.

9 But we saw and we believe the
10 evidence is uncontroverted that there
11 was significant risk around the
12 winddown.

13 The protection agreement
14 liabilities are going to be honored
15 in a sale transaction. In a
16 winddown, they would very likely be
17 rejected unless we could find
18 somebody to take those liabilities
19 and basically sell that part of the
20 business for zero or negative value.

21 THE COURT: While we're on this
22 subject of the potential warranty,
23 the protection agreements, there was
24 some discussion yesterday about the
25 risk that there would be a delay in

1 PROCEEDINGS

2 the approval of the KCD transfer.

3 MR. SCHROCK: Yes.

4 THE COURT: You have the PBGC
5 resolution somewhat ameliorates that
6 or more than somewhat, but you still
7 have to go to a third-party to get
8 approval. How is the risk allocated
9 in that approval?

10 MR. SCHROCK: Your Honor, we
11 handled that. If you take a look at
12 slide 27. Section -- this is section
13 2.8 E of the asset purchase agreement
14 which states that from the closing
15 date until such time as the transfer
16 of the KCD notes and assumption of
17 purchase agreement liability occurs,
18 the buyer provides services to the
19 applicable seller to sufficient to
20 enable the sellers to perform the
21 purchase agreement liabilities and in
22 consideration for such services the
23 sellers are paying to the buyer
24 amount equal to the aggregate amounts
25 paid by buyers and sellers with

1 PROCEEDINGS

2 respect to any licenses which buyers
3 licenses to KCD IP.

4 So effectively, instead of making
5 payments under the new KCD exclusive
6 license, the buyer is going to get to
7 keep it but that results in the buyer
8 paying for, during the interim
9 period, they're paying for and
10 bearing the economic risk associated
11 with the purchase agreement
12 liabilities. I'm sure ESL can stand
13 up and confirm that. And that amount
14 is in excess of the royalties that
15 would ever be paid during that
16 interim period.

17 So ESL, in short, ESL is bearing
18 the risk associated with the
19 administration, the purchase
20 agreement liabilities pending --

21 THE COURT: During that interim
22 period.

23 MR. SCHROCK: During that interim
24 period. The avoidance action, no
25 claims are being released in a

PROCEEDINGS

winddown, but of course there's a very limited release here. And we thought that was very meaningful to the estates, that the litigation is very largely preserved for the benefit of the estates. That was a key compromise that we came to in accepting the bid.

Mr. Basta will hit on the 507(B) claims and some of the nuances around the release. But the vendors of this company -- the company has in excess of 10,000 vendors. So when we talk about there's a couple of people, I think Mr. Burian mentioned that might be affected by this, by Sears closing, we big to differ. The company's schedules are on file. There's hundreds of millions of dollars in vendor claims. All of these parties have relationships with Sears. They will continue to have those relationships moving forward in very large part as a result of the

1 PROCEEDINGS

2 benefits of this deal.

3 The claims pool is very
4 substantially reduced. And if you
5 take a look at the next slide on
6 slide 16, we put this chart in our
7 reply but it bears emphasizing. When
8 you look at the recoveries to
9 creditors overall, there is a very
10 significant benefit in terms of the
11 reduction of the claims pool in
12 conjunction with this transaction,
13 even compared to a winddown, as well
14 as some creditors getting enhanced or
15 better treatment.

16 Now the committee --

17 THE COURT: This is before
18 litigation, any litigation with them?

19 MR. SCHROCK: That's right,
20 litigation is not included in these
21 recoveries, in either the committee's
22 or the company's charts.

23 But the winddown of this company
24 is uncontroverted. For the
25 committee, it's never been done.

1 PROCEEDINGS

2 From the company, you have witnesses
3 saying it's never been done. But we
4 would do our best to manage it.

5 We have a 465 (D) (4) deadline
6 that's on May 3rd. I think everybody
7 would try their best in the context
8 of a winddown. But when you have a
9 transaction like this that's on the
10 table that actually gives the company
11 a chance, and nothing is for certain,
12 but substantially reduces the claim
13 pool, treats creditors better, saves
14 45,000 jobs, judge, it's not close.

15 Now the sale transaction does not
16 guarantee administrative solvency.

17 It is certainly a very important
18 point for the company since the start
19 of these cases. It's not required to
20 sell assets. You don't have to have
21 administrative solvency. But we
22 believe we're administratively
23 solvent. I think under the debtors'
24 analysis the shortfall is \$42
25 million. We do not take into account

1 PROCEEDINGS

2 any litigation claims in considering
3 that. We have opportunities in
4 excess of \$100 million.

5 But in the context of a winddown,
6 you know, there's certainly,
7 according to Mr. Meghji, there's also
8 no guarantee that the company will be
9 administratively solvent.

10 But importantly, the sale
11 transaction we think gives us the
12 highest or best opportunity.

13 Mr. Transier talked about in
14 accepting the successful bid all of
15 the things that they looked at. The
16 nature and amount, the ability of
17 both parties to close, the recovery
18 of the successful bid would provide
19 to nonESL creditors liquidity, the
20 alternative to the successful bid
21 which is the winddown and the loss of
22 tens of thousands of jobs.

23 That alternative of liquidation,
24 in our judgment, after consultation
25 with numerous parties, was not in the

1 PROCEEDINGS

2 best interests of stakeholders.

3 Now Mr. Kamalani gave testimony
4 around adequate assurance of future
5 performance. It's worth noting that
6 adequate assurance does not mean
7 absolute assurance or guaranteed
8 performance.

9 They have a business plan. They
10 have financing. They have excess
11 availability at closing in excess of
12 \$400 million. They have a means and
13 a business plan to move this company
14 forward with a very substantially
15 reduced balance sheet, with much less
16 debt. They have a smaller footprint.
17 But they kept open the profitable
18 stores. And giving Sears a chance,
19 your Honor, we think it's more than
20 warranted under the facts that are
21 before the court.

22 We go through on the next couple
23 of slides, which I won't belabor,
24 just all of the uncontroverted
25 evidence that's in favor of adequate

1 PROCEEDINGS

2 assurance of future performance.

3 There's nothing out there that has
4 been put forth by the committee
5 that's really put this evidence into
6 serious question. And we do think
7 that the company's witnesses when
8 considered overall and the court were
9 to make a ruling, that the company's
10 witnesses have been interested,
11 dedicated. They are very credible.
12 And they were in the details compared
13 to the high level views that we
14 received from the unsecured
15 creditors' committee witnesses in
16 these cases.

17 Your Honor, overall I'm going to
18 cede my time and allow Mr. Basta to
19 come up here and say a few words
20 about the release. But we are very
21 much in favor of approval of this
22 sale.

23 We do need some guidance and
24 clarity from the court around the
25 \$166 million issue in the event that

1 PROCEEDINGS

2 we don't resolve it. We think the
3 issue is clear under the terms of the
4 document. But we're prepared to move
5 to closing providing that the debtors
6 are not liable. We provided the
7 agreements and \$166 million is
8 actually taken on by ESL. But I'm
9 happy to answer any further
10 questions. Otherwise I can cede the
11 podium and respond to any objections.

12 THE COURT: Okay. Thank you.

13 MR. BASTA: Good morning, your
14 Honor, Paul Basta from Paul, Weiss on
15 behalf of the restructuring
16 subcommittee.

17 Mr. Britton, my partner, will hand
18 up the clarifications to the ESL
19 release that were discussed on the
20 record in the beginning of the
21 hearing.

22 I think there's one or two issues
23 that the committee still has with the
24 language, and once that's done I'll
25 provide a closing statement on behalf

1 PROCEEDINGS

2 of the restructuring subcommittee if
3 that's okay with the court.

4 THE COURT: Okay.

5 MR. BRITTON: Good morning, your
6 Honor, Bob Britton of Paul, Weiss on
7 behalf of the restructuring
8 subcommittee. I have an amendment to
9 the asset purchase agreement that was
10 filed by the debtors this morning.
11 Revisions to the release provisions
12 of the APA are embodied in that
13 document. I have a copy here that I
14 can hand up to your Honor.

15 THE COURT: Okay.

16 MR. BRITTON: Your Honor, there's
17 a lot of changes in the amendment to
18 the APA capped for you at the back of
19 that document, a red line that just
20 goes to the release provisions that
21 fall within the mandate of the
22 restructuring subcommittee.

23 THE COURT: Okay.

24 MR. BRITTON: So the first thing
25 we're focused on, your Honor,

1 PROCEEDINGS

2 following the filing of the original
3 asset purchase agreement was ensuring
4 that the actual purchase of assets
5 didn't somehow cause ESL to purchase
6 claims and therefore get a back door
7 release, otherwise were carved out of
8 our release. So we started in the
9 acquired asset section of the APA and
10 that's in section 2.1 B. What we
11 provided here is that ESL, as part of
12 its commercial negotiation with the
13 larger restructuring committee,
14 negotiated the purchase ordinary
15 commercial claims with counterparties
16 it's continued to do business with
17 and we carved section 2.1 P that
18 required asset purchase of claims
19 back to essentially those claims and
20 then added clarifying language that
21 none of the excluded assets or
22 excluded liabilities are included in
23 those purchase of assets.

24 We also deleted section 2.1 T
25 which was largely duplicative of

1 PROCEEDINGS

2 section 2.1 P and also said that ESL
3 was buying claims and actions.

4 Then in section 2.2 I, your Honor,
5 which is the excluded assets we
6 provided that all claims, proceedings
7 and causes of action are excluded
8 assets other than those claims and
9 causes of action that are
10 specifically called out as an
11 acquired asset in section 2.1. We
12 also added clarifying language here
13 that nothing in this provision
14 affects the scope of the releases as
15 set forth in section 913.

16 That brings us to section 913,
17 your Honor. And so in section 913,
18 section B is the actual allowance of
19 the ESL funded debt claims per our
20 negotiation. We've added to that in
21 response to comments from your Honor
22 language that clarifies that the
23 allowance of any ESL claims, and ESL
24 claim is defined as the claims that
25 are -- the funded debt claims that

PROCEEDINGS

are allowed by the limited release,
the allowance of any ESL claim shall
not limit or preclude any claim under
any applicable law or doctrine of
collateral estoppel, res judicata,
claim or issue, preclusion or
otherwise.

Then you go to the actual release
which is really you have to go to the
definition of release of estate
claims in subsection E 2. And what
we've done here, your Honor, is
clarified again that the only claims
that are being released are claims
that could be brought to challenge
the allowance of the ESL claims. So
there are claims against ESL under
equitable principles of subordination
and recharacterization, under section
263 (K), 502 (A) or 510 (C) of the
bankruptcy code.

We've also provided your Honor
that any claims against buyer as a
momentary holder of the ESL claims

1 PROCEEDINGS

2 before the credit bid are being
3 released so that the only causes of
4 action that we will retain are
5 against ESL and ESL related parties.

6 The rest of this, that's really
7 the first five lines of the
8 definition.

9 The rest of this is for the
10 avoidance of doubt clarifying things
11 that are not included in the release
12 estate claims.

13 Among things that are not included
14 in the release estate claims are, and
15 I won't list them all but I'll call
16 out any claims for causes of action
17 constructive or fraudulent transfer
18 under 11 USC 544 B, 568 or 550 and
19 new clarifying language in the
20 parenthetical that says including,
21 but not limited to, any claims for
22 damages or equitable relief other
23 than disallowance of ESL claims.

24 What we've meant to clarify with
25 that language, your Honor, is that we

1 PROCEEDINGS

2 can bring fraudulent conveyance
3 claims related to ESL claims on the
4 debt claims that have been allowed.
5 The remedy just can't be avoidance of
6 those claims.

7 THE COURT: But this is all for
8 the avoidance of doubt.

9 MR. BRITTON: That's all for the
10 avoidance of doubt.

11 THE COURT: The first sentence is
12 the key sentence.

13 MR. BRITTON: Correct, your
14 Honor. NoW, the UCC, creditors'
15 committee and the Akin law firm sent
16 across comments as to these release
17 provisions last night. And we
18 incorporated certain of those
19 comments. I think we still have a
20 disagreement on at least one
21 substantive point which is that Akin
22 had asked us to include in this
23 release estate claim definition
24 language to the effect that the
25 debtors, the estates continue to

1 PROCEEDINGS

2 pursue claims for equitable
3 subordination and recharacterization,
4 provided that the only remedy on
5 account of those claims could be --
6 it wouldn't be disallowance of the
7 ESL claims, it would be presumably
8 damages against ESL.

9 Our view, your Honor, is two-fold.
10 One, at the subordination and
11 recharacterization our remedy is for
12 equitable conduct that will give rise
13 to money damages. But separately and
14 apart from that the inequitable
15 conduct that the committee is focused
16 on, we have preserved claims that
17 inequitable conduct -- in fact there
18 is inequitable conduct there. That's
19 included in the avoidance of doubt
20 language and that would include, your
21 Honor, claims for fraudulent transfer
22 and actual fraud.

23 And we intend to continue to
24 investigate and pursue those claims
25 on behalf of the estate.

1 PROCEEDINGS

2 But allowing the ability to
3 continue to pursue equitable
4 subordination and recharacterization
5 claims against ESL goes directly
6 contrary to the scope of the limited
7 release that we had negotiated with
8 them in order to allow the credit
9 bid. Thank you, your Honor.

10 THE COURT: Do you want to
11 address this now or later?

12 MR. QURESHI: Happy to address it
13 now, your Honor. For the record,
14 Abid Qureshi of Akin Gump on behalf
15 of the committee.

16 It is our view, your Honor, that
17 what is by design supposed to happen
18 with this release is no claims
19 against Newco, no claims against
20 their allowed claims, but in every
21 other respect we should be permitted
22 to pursue those claims against ESL.

23 So really the language that we
24 built into the release, your Honor,
25 was aimed at ensuring that the very

1 PROCEEDINGS

2 same remedy that one could get
3 against their claims for equitable
4 subordination or recharacterization,
5 should be a remedy that is available
6 to be pursued only as against ESL.

7 And that is what we tried to do
8 with the language that we suggested
9 and that is --

10 THE COURT: I'm sorry, is that
11 remedy -- that remedy is either a
12 subordination of the claim or
13 recharacterization of the claim.
14 It's not a damages remedy, right?

15 MR. QURESHI: Well, it's the
16 economic equivalent, your Honor.
17 That's the point.

18 THE COURT: But that's -- if it's
19 damages I understand it. But if it's
20 equitable subordination then by
21 definition it's a claim related
22 remedy.

23 MR. QURESHI: It's the measure of
24 damages on account of either
25 equitable subordination,

1 PROCEEDINGS

2 recharacterization. So as your Honor
3 is well aware, those are remedies or
4 causes of action I should say where
5 the court has great latitude in terms
6 of what the remedy is, how much of
7 the claim to subordinate, how much of
8 the claim to recharacterize.

9 What we are saying is we should be
10 able to pursue ESL for the dollar
11 equivalent, economic equivalent of
12 whatever that amount might be.

13 THE COURT: But I've never seen
14 -- by definition, that's not what
15 they are. Those remedies are claim
16 related remedies. I mean they affect
17 the defendant's claim as opposed to
18 -- affirmative claim. This preserves
19 equitable claims.

20 I mean it just doesn't preserve
21 equitable subordination which means a
22 claim is subordinated or
23 recharacterization which means the
24 claim is recharacterized either as an
25 equity interest or maybe as an

1 PROCEEDINGS

2 unsecured claim.

3 I mean I think the preservation of
4 equitable damages does what you want.

5 MR. QURESHI: Again, your Honor

6 --

7 THE COURT: Except to say it's
8 not -- it wouldn't be under the
9 rubric of equitable subordination.

10 I've never seen an equitable
11 subordination opinion that says that
12 you have to pay damages and
13 recharacterization that says you have
14 to pay damages. It just doesn't.

15 MR. QURESHI: Agreed. Again, the
16 purpose of the language we were
17 looking for was to preserve the
18 economic equivalent if you will of
19 whatever that remedy might be.
20 That's all that it was designed to
21 do.

22 THE COURT: But that's creating a
23 new -- the language that's in here
24 preserves equitable remedies other
25 than disallowing the claim or

1 PROCEEDINGS

2 subordinating the claim.

3 That to me is the economic
4 equivalent.

5 But to say that you're creating a
6 new form of equitable subordination,
7 I'm not prepared to do that. It's a
8 different -- that's like you're
9 asking me in a contract to say that a
10 remedy that is well defined is no
11 longer well defined and it's an
12 informative claim as opposed to a
13 reduction of a claim or
14 recharacterization of a claim.

15 MR. QURESHI: Your Honor, the
16 important point I think here is if
17 this court's reading of the language
18 that's been presented is that all of
19 the equitable claims as against ESL
20 and Mr. Lampert are preserved.

21 THE COURT: Well I said
22 resubordination or
23 recharacterization. Okay.

24 MR. BRITTON: Thank you, your
25 Honor. Unless your Honor has any

1 PROCEEDINGS

2 other questions about the scope of
3 the releases, I'm happy to cede the
4 podium.

5 THE COURT: I read them quickly
6 but I think they did the trick.

7 MR. BRITTON: Thank you, your
8 Honor.

9 THE COURT: I appreciate the
10 parties working on it to clarify.

11 MR. BASTA: Good morning, your
12 Honor, Paul Basta from Paul, Weiss on
13 behalf of --

14 THE COURT: I'm sorry to
15 interrupt you. So this language will
16 also be the language in the order as
17 far as Cyrus is concerned? When
18 people say it's the same thing,
19 that's what they mean?

20 MR. BASTA: Yes.

21 THE COURT: But it will be in the
22 order instead of this agreement.

23 MR. BASTA: The scope of the
24 Cyrus lease, although outside the
25 scope of the restructuring

1 PROCEEDINGS

2 subcommittee, will be and should be
3 the same as the scope of the ESL.

4 THE COURT: You may want to add
5 the MTN note language. It was MTN,
6 right? Okay.

7 MR. SINGH: Your Honor, Sunny
8 Singh for Weil. It's more general.
9 There's just a general reservation of
10 rights. We didn't go into all the
11 detail because it was a little less
12 prominent than the ESL piece but
13 there is a reservation.

14 THE COURT: The release is no
15 broader than as set forth in the
16 section.

17 MR. SINGH: Right. We can add.

18 MR. BRITTON: I think you can put
19 it in the MTN too.

20 THE COURT: Yes, you should put
21 it in the MTN too.

22 MR. BRITTON: And I'll just
23 confer with counsel.

24 MR. BASTA: Your Honor, Paul
25 Basta from Paul, Weiss on behalf of

1 PROCEEDINGS

2 the restructuring subcommittee. I
3 will try to avoid any overlap with
4 Mr. Schrock. This subcommittee
5 statement, your Honor, Mr. Schrock
6 walks through the execution risks
7 associated with this deal. Our
8 subcommittee statement is predicated
9 on ESL not reneging on the \$166
10 million assumption. That was a
11 critical component of the
12 subcommittee's decision to provide
13 the credit bid release. And so this
14 statement is on the assumption that
15 ESL is going to honor the agreement
16 in that respect.

17 The decision before the
18 restructuring subcommittee in this
19 case was whether to provide a release
20 to ESL in order to facilitate a going
21 concern transaction that would
22 maximize --

23 THE COURT: I'm sorry. Can I
24 interrupt you. Let's assume -- I
25 hope this doesn't happen. I assume

1 PROCEEDINGS

2 it won't happen but just
3 hypothetically assume that the deal
4 closes, ESL doesn't reimburse for the
5 debts listed on schedule 1.1 G, it's
6 ultimately determined that the deal
7 is breached.

8 MR. BASTA: By ESL.

9 THE COURT: Is there the release
10 -- release isn't effective at that
11 point?

12 MR. BASTA: It is not effected.
13 We wanted to effect the -- when we
14 looked at the release, for a long
15 time the release was on the back
16 burner. Because the concept here was
17 we needed a deal. We needed a viable
18 deal. It only makes sense to talk
19 about a release in connection with
20 the viable deal. So the 166 from the
21 subcommittee's perspective was
22 critical to get to a deal that was
23 viable and the release was predicated
24 on that assumption.

25 THE COURT: Okay.

1 PROCEEDINGS

2 MR. BASTA: So the decision
3 before the subcommittee was whether
4 to provide a release to ESL in
5 whatever form we could negotiate in
6 order to facilitate a going concern
7 transaction or alternatively to
8 choose liquidation. That was it.

9 Release, deal, or liquidation.

10 And ultimately the restructuring
11 subcommittee determined in good faith
12 to approve a limited credit bid
13 release to facilitate a
14 reorganization and came to the view
15 that that was better for the estates
16 than proceeding to a winddown.

17 THE COURT: I think I have the
18 chronology here. But all of the ESL
19 proposals that the restructuring
20 committee, the subcommittee rejected
21 contained a general release, right?

22 MR. BASTA: Yes, and let me walk
23 through that.

24 THE COURT: The one that was
25 accepted had this limited release.

1 PROCEEDINGS

2 MR. BASTA: Right. Your Honor,
3 if I can walk you through that for
4 one second. On December 5th, 2018
5 was the first indicative bid by ESL
6 and it contained a broad ESL release.
7 And on December 9th and 12th it was
8 rejected in writing by both the
9 restructuring committee and the
10 subcommittee.

11 On December 28th bid by ESL, it
12 contained a broad release and it was
13 rejected on January 4th.

14 On January 6th bid there was also
15 a -- there was also a broad release
16 and it was rejected on January 6th.

17 On January 7th Cleary sent a
18 letter threatening the restructuring
19 subcommittee with breach of fiduciary
20 duty if they did not accept the ESL
21 bid.

22 On January 9th ESL put a bid on
23 the auction record and we rejected it
24 because it contained a broad release
25 among other things.

1 PROCEEDINGS

2 It wasn't until January 15th, late
3 in the evening -- I'm sorry, on
4 January 15th there was yet another
5 bid that also contained a broad
6 release that was rejected by the
7 subcommittee.

8 It wasn't until the limited
9 release was accepted by ESL and other
10 components of the deal were improved,
11 that the subcommittee agreed to
12 provide the limited release.

13 And we believe that the limited
14 release is the solution to this case.

15 If your Honor remembers, in the
16 early bidding procedures there was a
17 requirement that in order to credit
18 bid, ESL was going to have to cash
19 backstop any credit bid. And that
20 was where we were for a long time.
21 And ESL indicated there would be no
22 going concern with a cash bid.

23 So we had to figure out a way to
24 facilitate a credit bid if we wanted
25 to achieve the benefits of the going

PROCEEDINGS

concern, and so we came up with the bifurcated structure. And the bifurcated structure is one where we retained the valuable causes of action while allowing the company to receive the benefits of a reorganization. We think that's the lynchpin of the case and the obvious benefit of moving forward.

There were a number of, your Honor, of less obvious benefits that came out of the subcommittee's negotiations around the credit bid. The credit bid was the key, and there were substantial improvements to the deal in addition to the limited release that stemmed from that credit bid negotiation.

They closed the administrative insolvency gap by hundreds of millions of dollars. The deal provides in our view, when we looked at this we always look at is the going concern better than the

1 PROCEEDINGS

2 winddown, not is the going concern
3 good. Is it, does it provide
4 proportionally an incrementally
5 better alternative?

6 Our analysis showed that in the
7 final bid that third party secured
8 creditors are benefited compared to a
9 winddown and that's not including
10 obviously ESL to the tune of \$152
11 million.

12 It's our analysis that general
13 unsecured creditors that are getting
14 assumed under the deal which include
15 protection agreement and other
16 consumer related claims of \$524
17 million, are getting paid under this
18 deal and they would not get paid in a
19 winddown. I'm going to get into some
20 more detail about that later.

21 But earlier iterations of the
22 contract from ESL added a condition
23 to the assumption of the protection
24 agreement liabilities that they be
25 reaffirmed by the consumer. And we

1 PROCEEDINGS

2 were able to get that out of the
3 contract to make that an absolute
4 requirement to assume those
5 liabilities. And that allowed us to
6 value that as a contribution to the
7 estates.

8 There's a \$621 million avoidance
9 of additional administrative claims
10 in a reorg versus a winddown which we
11 think is very significant and there
12 are jobs that are being preserved.

13 There's also a substantial
14 limitation on ESL's ability to
15 recover from litigation proceeds with
16 respect to its deficiency claims. We
17 negotiated so there would be no right
18 of ESL to share on any Land's End or
19 Seritage litigation, no right of ESL
20 to share on any litigation relating
21 to any ESL misconduct and we were
22 able to cap ESL's 507(B) claim at \$50
23 million which so if there's other
24 nonESL litigation recovery, their
25 507(B) claim is capped.

1 PROCEEDINGS

2 The decision to provide the
3 limited release is coming from a
4 process where Mr. Carr and Mr.
5 Transier faithfully discharged their
6 fiduciary duties. There is some
7 allegation in the committee's papers
8 that Mr. Carr and Mr. Transier were
9 handpicked by Mr. Lampert. There's
10 no evidence in the record to support
11 that. In fact, the evidence in the
12 record is that they were introduced
13 to the board by Mr. Schrock and that
14 they had -- the evidence is clear
15 that they have no prior relationships
16 with ESL.

17 Your Honor observed the demeanor
18 of Mr. Transier and Mr. Carr in
19 person and I think anyone who watched
20 that testimony would see that they
21 were not pulling any punches
22 whatsoever and were faithfully trying
23 to do what was best for the estate.

24 And of course Mr. Carr and Mr.
25 Transier have found that there's

PROCEEDINGS

hundreds of millions of dollars of
valuable claims against ESL and
repeatedly rejected ESL's bids that
contained a release, even in the face
of litigation threats from ESL.

It's also unmistakable that Mr.
Carr and Mr. Transier satisfied the
duty of care. The debtor set up a
purely independent subcommittee
because it could see what was coming
down the pike and if there was any
way to get this through given the
conflicts involved you needed a truly
independent committee.

And Mr. Carr and Mr. Transier
directed all of the professionals for
the subcommittee, including A&M and
Evercore to do a massive amount of
work investigating the claims up
front so that we would be in a
position at the auction to assess the
value of those claims, and all of
that work led to the bifurcation
approach that was an informed

1 PROCEEDINGS

2 approach so we could present to this
3 court a solution that would allow a
4 reorganization instead of making a
5 liquidation a fait accompli.

6 Mr. Schrock talked about the 58
7 restructuring committee meetings,
8 many of which the subcommittees'
9 professionals attended. There were
10 also three times a week calls of the
11 subcommittee and a myriad of other
12 one-off conversations on the process.

13 Mr. Carr and Mr. Transier, as you
14 could see, were not passive
15 recipients of professional advice.
16 They were deep in the weeds on what
17 the numbers are.

18 The committee presented the court
19 with -- the committee presented the
20 court with texts of Mr. Carr. What
21 those texts showed is that Mr. Carr
22 wanted to get to the right answer and
23 was not satisfied with the numbers
24 that were coming out of the
25 professionals upon which to make a

1 PROCEEDINGS

2 decision so he didn't make a decision
3 until those numbers settled down.

4 That is the embodiment of satisfying
5 the duty of care.

6 Your Honor, I have two slides I'd
7 like to hand up.

8 Mr. Carr and Mr. Transier had a
9 deep understanding of what fiduciary
10 duty means in an insolvency
11 situation.

12 If you look I've given your Honor
13 a quote from the Gewala. This is of
14 course the seminal decision where
15 this is arising in the context where
16 the Delaware Supreme Court is
17 concluding that there's no separate
18 duty, fiduciary duty of afforded to
19 creditors. If your Honor reads the
20 sentence it says, to recognize a new
21 right for creditors to bring direct
22 fiduciary duty claims against those
23 directors, would create a conflict
24 between those directors' duties to
25 maximize the value of the insolvent

1 PROCEEDINGS

2 corporation for the benefit of all
3 those having an interest in it, in
4 the newly directed fiduciary duty to
5 individual creditors.

6 This is a sophisticated sentence
7 that understands the difficult job
8 that directors have to undertake
9 because there are numerous
10 constituents that have an interest in
11 the corporation. So by saying you
12 have a duty to the corporation, you
13 have to take into account the impact
14 on all of the constituents. And this
15 is different than a creditors'
16 committee who has duty to its
17 unsecured creditor constituent.

18 And so if you look at it through
19 that lens where the restructuring
20 subcommittee had a broader
21 constituency group to consider than
22 the unsecured creditors' committee,
23 I've given the court a slide that
24 talks about the release consideration
25 that we considered separate for the

1 PROCEEDINGS

2 reason to provide the limited
3 release.

4 And if you go through this, your
5 Honor, I think it's very compelling.
6 We're getting \$35 million of cash.
7 We're getting \$152 million of third
8 party secured creditors. We're
9 getting \$453 million of assumption
10 for protection agreement liabilities.
11 We're getting gift card liability
12 assumption of \$13 million. We're
13 getting \$68 million of assumption of
14 Shop Your Way liabilities. We're
15 avoiding \$621 million of
16 administrative expense claims.

17 We are preserving the litigation
18 against ESL and other defendants.
19 We're getting a cap on ESL recoveries
20 and we're preserving tens of
21 thousands of jobs.

22 THE COURT: Other than the cap
23 this is part of the sale
24 consideration, your point is that the
25 sale wouldn't have happened without

1 PROCEEDINGS

2 the credit bid?

3 MR. BASTA: To get a release
4 under Drexel, there needs to be
5 consideration. There needs to be
6 consideration it needs to be more
7 than the winddown.

8 THE COURT: Well --

9 MR. BASTA: So in other words, if
10 they showed up with a deal --

11 THE COURT: The winddown includes
12 what you carved out of the release.
13 I guess I'm looking at this a little
14 differently, which is that there's
15 value that ESL is paying for the
16 debtors in addition to the credit
17 bid.

18 But I view that as value that I
19 would measure against a winddown.
20 The alternative.

21 I wouldn't also measure it as
22 consideration for the limited
23 release. But I understand your point
24 which is that value wouldn't be there
25 without the limited release. Which

1 PROCEEDINGS

2 is a little bit of a different thing.

3 MR. BASTA: Your Honor I
4 respectfully disagree. If they
5 showed up with \$35 million for the
6 credit bid release, we would not have
7 provided it.

8 THE COURT: Because the whole
9 deal wouldn't have made sense.

10 MR. BASTA: The whole deal
11 wouldn't have made sense and the
12 whole deal wouldn't have been better
13 than a liquidation.

14 THE COURT: Right.

15 MR. BASTA: You had to measure
16 whether to give the release on
17 whether there were benefits to the
18 company above a liquidation.

19 THE COURT: And it's a limited
20 release.

21 MR. BASTA: And it's a limited
22 release. And so I think the question
23 that I'd like to focus in conclusion,
24 your Honor, is why does the
25 subcommittee value these things as

1 PROCEEDINGS

2 important but the creditors'
3 committee does not value them as
4 important? Because I think that's
5 the key as to what's really going on
6 in this case.

7 If your Honor looks at whatever
8 the committee, creditors' committee
9 describes this deal, they say it's
10 \$35 million for the release. They
11 never acknowledged that there are
12 very significant unsecured creditor
13 constituencies that are doing better
14 in this deal than what they would do
15 in a winddown. In a winddown the
16 protection agreement liabilities
17 would not get paid. Gift card,
18 consumer, jobs. In fact, Mr. Burian
19 said that the creditors' committee is
20 not supposed to look at jobs. I
21 guess he views employees, I think he
22 said they're not prepetition
23 creditors or that in our vibrant
24 economy they can go and find another
25 job. So he didn't even view them as

1 PROCEEDINGS

2 a constituency that the unsecured
3 creditors' committee in its lens
4 needs to, needs to consider.

5 And I think this is the key, is
6 why doesn't the committee view these
7 benefits as being important enough to
8 support this deal?

9 And I want to suggest to the court
10 that there are four reasons and that
11 none of those reasons warrant denial
12 of this transaction.

13 The first is that none of the
14 unsecured creditors that are on this
15 list as receiving a benefit are on
16 the committee.

17 The committee is not dominated by
18 trade. It is not -- it does not have
19 employee representatives. It does
20 not have consumer representatives.

21 The committee constituency is not
22 actually getting these benefits.

23 The second reason I think is that
24 I think the creditors' committee is
25 focused on equitable subordination as

1 PROCEEDINGS

2 an important remedy for them because
3 they can hold that debt essentially
4 in the case and recover from the
5 liquidation proceeds and subvert the
6 priority scheme.

7 And I understand that as an
8 important consideration for the
9 committee. But from our perspective,
10 when we've preserved our remedies by
11 preserving the litigation, we don't
12 think that preserving equitable
13 subordination as an independent
14 remedy is a reason to thwart
15 reorganization.

16 The third argument they made and
17 your Honor asked Mr. Schrock about it
18 relates to the unencumbered real
19 estate value. And in a liquidation
20 if you believe that the unencumbered
21 real estate value could get a lot of
22 value, then your whole analysis as to
23 whether reorg versus winddown would
24 change. But the way the subcommittee
25 looked at that is that in the

PROCEEDINGS

winddown analysis the unencumbered real estate was consumed by the newly created administrative claims.

So the way we looked at it is when you compared the two transactions, the unencumbered property wouldn't flow down to unsecured creditors to give them a recovery.

Now I understand that there's a debate about what the value of that is. But the restructuring committee's professionals reported on what their view of the valuation of those assets was and that that value would not result in -- would not result in a recovery to the unsecureds.

THE COURT: Unless you hit a home run.

MR. BASTA: Unless you hit a home run.

THE COURT: Well not on the real estate, on the litigation against ESL including under section 507 (D) and

1 PROCEEDINGS

2 506 (C) .

3 MR. BASTA: Yes.

4 THE COURT: They basically assume
5 out a claim. There would be a super
6 priority claim under 507 (D) .

7 MR. BASTA: Right.

8 And then the last thing that I
9 think they're focused on is they say
10 they don't believe in Newco. And if
11 you don't believe in Newco then maybe
12 the benefits that we are considering
13 that would be assumed by the new
14 company shouldn't be valued because
15 the company is not going to survive.

16 I would say while they have
17 questioned it, at no point in the
18 process has the unsecured committee
19 ever said this deal gives valuable
20 consideration to some of our
21 constituencies. Let us work the
22 contract to make the contract better,
23 to preserve these, better to preserve
24 these benefits. The entire time
25 their focus has really been on just

1 PROCEEDINGS

2 causing a liquidation. They
3 announced that in the very beginning
4 of the case.

5 Irrespective of that --

6 THE COURT: Maybe here that's the
7 best negotiating strategy but we can
8 leave that for business schools.

9 MR. BASTA: We can leave that for
10 another day. I would say, your
11 Honor, that the subcommittee's
12 professionals and the restructuring
13 committee professionals believe that
14 there's a reasonable prospect that
15 Newco can succeed and that in light
16 of all the benefits that are -- that
17 can be achieved and the retention of
18 the litigation that it should be
19 approved.

20 Three legal points and then I'll
21 sit down.

22 We're going to defer to the
23 restructuring committee on standard
24 of review. We would point out, your
25 Honor, that even if the court applied

1 PROCEEDINGS

2 the entire fairness test to this
3 transaction, we think that this is
4 entirely fair. There's been
5 tremendous court oversight through
6 the entire process. We have a truly
7 independent subcommittee and we
8 believe that entire fairness test is
9 about a fair process and fair price
10 and given the auction process as well
11 as the transparency with all parties,
12 that even if entire fairness test
13 applies it has been satisfied.

14 Two cases I want to refer the
15 court to as your Honor considers
16 this. The first of the cases that
17 says that the estate has the right to
18 settle 502 (D) or release 502 (D)
19 claims, it is -- there was some
20 reference in the committee objection,
21 it is in re Foundation of New Era
22 Philanthropy 1996 Bankruptcy, Lexis
23 1829, 1996.

24 And the second is the Applied
25 Theory case from the Second Circuit

1 PROCEEDINGS

2 which holds that equitable
3 subordination claims are derivative,
4 especially in the context of where
5 the complaint that is the grounds for
6 equitable subordination harmed all of
7 the creditors equally.

8 And therefore our view is that we
9 have an ability, as because they are
10 derivative, they belong to the estate
11 to release them or settle them as
12 part of this transaction.

13 THE COURT: Okay.

14 AUDIENCE MEMBER VIA PHONE: Your
15 Honor, for the benefit of the sellers
16 that have objections in the agenda
17 that have not been disposed of, will
18 we have an opportunity to address the
19 court regarding those objections?

20 THE COURT: Yes, you will.

21 AUDIENCE MEMBER VIA PHONE: Thank
22 you, your Honor.

23 MR. BROMLEY: Good morning, your
24 Honor, Jim Bromley from Cleary
25 Gottlieb on behalf of ELS. I stand

1 PROCEEDINGS

2 here before you today, your Honor, as
3 an advocate to ask you to approve the
4 transaction that's before you.

5 I can't help, however, but feeling
6 a little bit like a character from
7 that Monte Python skit where somebody
8 walks in looking for an argument and
9 he finds himself getting hit on the
10 head lessons.

11 This is a difficult exercise, your
12 Honor. We are being criticized both
13 by the creditors' committee and to a
14 certain extent on the \$166 million
15 issue by both the debtors and the
16 subcommittee.

17 It is true that what happened in
18 this case from the very beginning was
19 that ESL has indicated very clearly
20 that it was interested in a going
21 concern transaction. It is also very
22 true that from the very beginning ESL
23 indicated that it wanted releases in
24 connection with pursuing that and the
25 ability to credit bid.

PROCEEDINGS

ESL lent the company over \$2.6 billion in the prepetition period, of which about \$2.4 billion was secured.

The vast majority of that effort was -- well the entire majority of that effort was made to keep this company in business and to allow it to avoid the very fee frenzy that we are facing here today in the bankruptcy court.

But while it might have been on a back burner for Mr. Basta, it is important for everyone to realize it was on the front burner for ESL. ESL has been criticized substantially and consistently throughout the case by creditors' committee and it is important for us to state on the record that we uncategorically deny any of the allegations that were made. We believe that the releases that are being provided are appropriate under the circumstances and we also believe that the claims

1 PROCEEDINGS

2 being retained are worthless.

3 So from an administrative solvency
4 perspective, your Honor, we don't
5 believe that the claims retained have
6 any value. We understand that
7 there's a difference of opinion
8 there.

9 But it is important that before we
10 go any further that that claim
11 position be made clear.

12 I'd like to turn to the \$166 --
13 yes, you have something to say, your
14 Honor?

15 THE COURT: No, go ahead.

16 MR. BROMLEY: I thought you had a
17 question. With respect to the \$166
18 million, both Mr. Basta and Mr.
19 Schrock made comments that were
20 somewhat inconsistent.

21 First they said they believe the
22 contract is in their favor and they
23 are ready to close. And then they
24 said they're ready to close so long
25 as your Honor gives some guidance or

1 PROCEEDINGS

2 makes some kind of decision that
3 indicates that they are right and we
4 are wrong.

5 We are ready to close based on the
6 contract as written, regardless of
7 the ultimate interpretation. But we
8 believe that the ultimate
9 interpretation is not for here today.

10 THE COURT: I don't have the
11 authority to decide that issue
12 although I do have to evaluate as in
13 essence whether it's reasonable to
14 assume the debtors' interpretation
15 because it's clear to me that the
16 debtors don't believe that the deal
17 is worth pursuing lest their
18 interpretation is right. So I'm not
19 able to make a decision today because
20 as the Second Circuit held in Orion
21 Pictures, but on the other hand it
22 needs to be evaluated as
23 Judge Chapman recently did in one of
24 her cases.

25 MR. BROMLEY: It's in that

1 PROCEEDINGS

2 context that I feel I need to address
3 it, your Honor, to a certain extent.

4 There are lots of information that is
5 not before the court. But what is
6 before the court is the contract and
7 the schedules. With great fanfare
8 the debtors today told you what is on
9 schedule 1.1 G which is the number
10 \$166 million.

11 That I think is fair to say not
12 particularly enlightening guidance as
13 to the specific accounts payable that
14 are supposed to go forward. And that
15 is exactly the issue.

16 The way the contract is written,
17 your Honor, and the way our bid
18 letter went in, the way Mr. Kamlani
19 testified, consistently from our
20 perspective, is that with respect to
21 the \$166 million, it's about accounts
22 payable with respect to product that
23 is ordered before the closing and
24 delivered after the closing.

25 THE COURT: Well it just doesn't

PROCEEDINGS

say that.

MR. BROMLEY: Well, your Honor,
actually we believe it does.

THE COURT: Okay, the schedule
doesn't.

MR. BROMLEY: The schedule has to
be read together with 1.1 F and 1.1 G
and they both say 166 million.

THE COURT: And other payables.

MR. BROMLEY: And other payables.

THE COURT: The definition refers
you to the schedule.

MR. BROMLEY: And ordered
inventory the way the line is
written, ordered inventory in our
view is clearly included in other
payables.

So with that, your Honor,
regardless of the ultimate outcome
ESL stands before you today ready to
close on the basis of the contracts
assigned.

With respect to the arguments that
have been made and will be made, I

1 PROCEEDINGS

2 think that there's a couple of points
3 that we want to add to those that
4 have been made by Mr. Schrock and Mr.
5 Basta.

6 When viewed through the
7 appropriate lens, your Honor, there's
8 really no question that all the
9 standards for approval have been met
10 and exceeded in this case.

11 For a buyer, one of the most
12 important aspects of the sale order
13 is defined in good faith. And with
14 respect to a finding of and with
15 respect to a participant in these
16 proceedings like ESL it is important,
17 critically important because of all
18 the allegations that have been made
19 against it.

20 THE COURT: What is it?

21 MR. BROMLEY: Good faith.

22 THE COURT: I just didn't hear
23 you.

24 MR. BROMLEY: Sorry, your Honor.
25 And the evidence is replete with

1 PROCEEDINGS

2 evidence -- the record is replete
3 with evidence of good faith, that
4 from the very beginning, prior to the
5 petition date, Mr. Lampert had been
6 the CEO resigned. The restructuring
7 committee was appointed. The
8 restructuring committee and the
9 subcommittee in particular was vested
10 with dual roles to both investigate
11 potential claims that may exist as
12 well as to evaluate any transactions
13 that would involve ESL.

14 And there's no evidence at all in
15 the record that anything happened
16 where either Mr. Lampert, Mr. Kamlani
17 or anyone else representing ESL had
18 any influence over the debtors'
19 process, any influence over the
20 debtors' business plan, any influence
21 over the debtors at all.

22 Indeed, your Honor, if anything,
23 the evidence is overwhelming with
24 respect to the intensity of these
25 negotiations.

1 PROCEEDINGS

2 This is a deal that has fallen
3 apart and come together on numerous
4 occasions. The intensity and frankly
5 contentiousness of the negotiations
6 that have taken place are marked.
7 They are, when at least two of the
8 witnesses, Mr. Transier, Mr. Kamrani
9 referred to the auction as a
10 four-day/night, that clearly is a
11 perfect encapsulation of the exercise
12 that went on during that week at Weil
13 Gotshal's offices.

14 Our offers were rejected
15 repeatedly. They were rejected
16 formally and informally. And at
17 every moment in time we came back to
18 the table and put more consideration
19 on the table.

20 With respect to the releases we
21 did start off looking for a global
22 release. That was our intention from
23 the beginning and that was our
24 desire.

25 As the transaction continued to

1 PROCEEDINGS

2 move forward, we understood that in
3 order to make this get over the
4 finish line that we needed to
5 identify an opportunity to negotiate
6 a more limited release and it was in
7 that context that on the night of the
8 15th and into the early morning of
9 the 16th that we sat down and were
10 able to cut that deal.

11 It is what is reflected in the
12 document. It's reflected in the
13 comments of Mr. Britton and certainly
14 with respect to the attempt by the
15 creditors' committee to recapture
16 certain of the release elements
17 particularly with respect to
18 equitable subordination and
19 recharacterization of this allowance,
20 we reject that entirely. That's not
21 the deal. And we have to have the
22 ability to credit bid or the
23 transaction cannot go forward.

24 And that includes frankly the
25 release -- the allowance of the

1 PROCEEDINGS

2 claims in their entirety.

3 The cabining of the opportunities
4 for those claims to recover that Mr.
5 Basta described were hard fought
6 negotiations and provide we believe
7 both protection for the estates as
8 well as protection for ESL.

9 But it was protection that was
10 hard fought in the context of a
11 global transaction.

12 Your Honor, you've heard from Mr.
13 Kamlani who is the president of ESL
14 with respect to the business plan and
15 there's been a lot made by the
16 creditors' committee about the
17 going-forward business plan of Newco.

18 The criticisms of the business
19 plan I think are important to take
20 for a moment.

21 One of the -- the creditors'
22 committee frankly rely almost
23 entirely on their purported expert
24 Mr. Kniffen. He did not appear in
25 court. He was not cross examined.

1 PROCEEDINGS

2 The parties have relied on the
3 designations of his testimony.

4 But I think it is important to
5 look at those designations because
6 Mr. Kniffen is by no, in no way,
7 shape or form an expert on anything.
8 Mr. Kniffen is a pundit on cable TV.
9 He has worked in the retail industry
10 but hasn't been involved in any way,
11 shape or form for about 15 years.

12 And he hasn't even set foot in a
13 Sears store in a year and a half at
14 least.

15 His expert opinion is no more
16 worthwhile than if we brought in a
17 parade of Sears customers who said
18 they like Sears, they like Kenmore
19 products and they enjoy shopping at
20 Sears.

21 And when you take Mr. Kniffen off
22 the table we believe he wouldn't
23 survive a Daubert challenge in any
24 circumstance so we did not bore the
25 court with it. You have simply

1 PROCEEDINGS

2 nothing on the side to criticize the
3 going-forward business plan.

4 Mr. Diaz as well relies almost
5 entirely on Mr. Kniffen's
6 assumptions. He does the math for
7 Mr. Kniffen. But if it wasn't for
8 Mr. Kniffen there would be no math
9 for Mr. Diaz to do.

10 And so if you take both Kniffen
11 and Diaz off the table which we
12 believe is appropriate in light of
13 Mr. Kniffen's obvious incapacity to
14 be qualified as an expert, there's
15 simply no evidence whatsoever that
16 the business plan for Newco going
17 forward is anything other than
18 appropriate.

19 Notwithstanding that, your Honor,
20 Mr. Kamalani was very clear as to the
21 opportunities that are being provided
22 with respect to the go-forward
23 business plan. The go-forward
24 business plan is not a plan to close
25 stores and fire employees. The

1 PROCEEDINGS

2 go-forward business plan is a plan to
3 maximize the opportunities provided
4 by the Sears ecosystem. That
5 includes the Innovel and SHS, Sears
6 Home Services network, to transition
7 from larger footprint stores to
8 smaller footprint stores, and to
9 transform this company, to transform
10 this company which is exactly what
11 ESL has been trying to do for the
12 past 13 or 14 years.

13 Now the fact that the company has
14 not succeeded is obvious because
15 we're here in bankruptcy court.

16 But when we're looking at
17 commitment of ESL to Sears, it's
18 important to contrast the commitment
19 of ESL to Sears and the commitment of
20 others in other situations. There
21 was testimony yesterday about Toys 'R
22 Us. The private equity sponsors in
23 Toys 'R Us did a leveraged buyout of
24 the company and abandoned it. Mr.
25 Lampert and ESL have been with Sears

1 PROCEEDINGS

2 and believers in Sears long term,
3 contrarian investors and they are
4 continuing to put money and resources
5 behind this business model and this
6 plan.

7 Now we can sit here and criticize
8 that business decision. But we
9 should not misinterpret that business
10 decision for some kind of evil
11 intent.

12 Mr. Lampert's dedication and ELS's
13 dedication to Sears really is without
14 question.

15 And the idea that we're doing
16 anything other than to try and make
17 this company succeed and succeed
18 going forward is completely belied by
19 the other options on the table.

20 If this was an exercise in trying
21 to obtain real estate and liquidate
22 that real estate, we would simply be
23 credit bidding the liens that we have
24 with respect to the real estate.

25 If this was an exercise to keep

1 PROCEEDINGS

2 Sears alive to protect our investment
3 in Seritage, there would have been no
4 reason to have put \$2.5 or 6 billion
5 into Sears instead of into Seritage,
6 the rest of which was only about \$750
7 million.

8 We are dealing with a universe of
9 incompatible positions, right. The
10 creditors' committee right now says
11 we are getting too much value and
12 we're not paying enough for it.

13 And at the same time they're
14 saying that that very Newco that's
15 getting too much value and not paying
16 enough for it is going to fail
17 because it's inadequately capitalized
18 and incapable of providing adequate
19 assurance of future performance.

20 Quite simply, the creditors'
21 committee can't have it both ways.
22 We can't be stealing assets and
23 unable to pay our creditors when
24 those debts come due going forward.

25 We're doing nothing with respect

1 PROCEEDINGS

2 to taking the assets other than to
3 incorporate them into a valid and
4 viable going forward business.

5 And every time the creditors'
6 committee stands up and talks out of
7 both sides of its mouth we have to
8 recognize it for what it is, right.
9 Creditors' committee is dominated by
10 Simon Properties, the largest real
11 estate mall owner in the country.
12 And what are we doing? We're sitting
13 here criticizing the real estate sale
14 process?

15 I submit, your Honor, that Simon
16 knows more and better about every one
17 of the properties in their malls than
18 anyone else including Sears.

19 So if they wanted to be here and
20 be bidding against this transaction,
21 they had every opportunity. And that
22 goes for every other large real
23 estate developer.

24 The idea that this Sears process
25 has been going on under some sort of

1 PROCEEDINGS

2 cover of darkness is just ridiculous.

3 Sears has been under a microscope
4 for years. Mr. Lampert has been
5 under a microscope for years. This
6 entire bankruptcy has been under a
7 microscope with live vlogging the
8 moment anything is said including
9 instantaneous reports of anything
10 going on in chambers conferences we
11 find outrageous.

12 There's nothing hidden in this
13 case. Any time something is said it
14 is broadcast almost immediately. And
15 the idea that we are doing something
16 undercover of darkness is frankly
17 outrageous.

18 Now, your Honor, I want to talk a
19 little bit about the reasonableness
20 of the settlement and the 9019
21 standards.

22 I know Mr. Basta covered it and
23 Mr. Britton described the release.

24 But it is very important that when
25 we're taking a look at this that

PROCEEDINGS

we're not conflating things, right.

The 9019 standard for approval of a settlement, which we understand is part and parcel of 363 standard for the sale, is such that you have to take into account the strength of these claims, but not have a mini trial with respect to the claims.

You have heard from Mr. Carr, from Mr. Transier, you've seen what was submitted by the restructuring subcommittee, that they have conducted an extensive investigation. They have taken a look at these equitable subordination, disallowance and recharacterization claims and they have come to a reasoned conclusion that the consideration being provided both in the form of the \$35 million as well as all of the other assumptions of liabilities is more than enough to justify this release.

I think it's important for a

PROCEEDINGS

moment to stop and go back to Mr. Basta's timeline. It is true, absolutely, we wanted a complete release all through the process. We did not get to the point where we were willing to engage on a more limited release until the time of the auction.

And it was in that same period of time, in conversations with the debtors and the subcommittee, that ESL did two things. One, decided that it would be willing to put a proposal on the table or consider a proposal, depending on which point of view you have, with respect to a more limited release. But at the same time also assuming substantial amounts of liability, substantial amounts of liability and increasing the overall value.

Mr. Kamlani testified yesterday, uncontradicted, that the bid that went in on the 28th of December, the

1 PROCEEDINGS

2 bid deadline, compared to the bid
3 that was accepted, had a difference,
4 a positive increase in value of \$800
5 million.

6 So between the time that our bid
7 went in on the 28th and the winning
8 bid was selected in the early morning
9 hours of the 16th, subject to
10 documentation, we did two things. We
11 increased the amount of consideration
12 by approximately \$800 million and we
13 also agreed to the more limited
14 release.

15 Now with respect to those -- and
16 this -- a lot of this ties into all
17 different pieces. But another piece
18 of this is that at the same time we
19 were assuming liabilities we were
20 addressing issues that dealt with the
21 so called allocation with respect to
22 unencumbered assets.

23 I think your Honor's math is
24 exactly right. We've got \$5.2
25 billion of consideration, \$1.3

1 PROCEEDINGS

2 billion of credit bidding, so that
3 consists of 3.9 of other
4 consideration.

5 But just to put a finer point on
6 that to give you a couple of other
7 datapoints. The protection
8 agreements that have been discussed,
9 what are the protection agreements
10 and what is the value with respect to
11 that?

12 It was in the context of that
13 December 28th to January 17th period
14 that we increased our bid to take on
15 responsibility for the entirety of
16 the protection agreements.

17 The protection agreements are if
18 you go and buy a washing machine at
19 Sears and they ask if you want an
20 extended warranty and you say yes and
21 you pay \$300 for it, something along
22 those lines, that is an obligation of
23 Sears to continue to provide service
24 and to come out to your home, fix
25 these appliances to the extent they

PROCEEDINGS

break.

Like any insurance, it's a bet, it's a bet that the quality of the product is going to be such that you're not going to have to spend nearly as much repairing the appliance as you did to buy it -- to buy the protection.

And so the accounting for these is obvious when they describe it but a little tricky from a distance.

There's about a billion dollars worth of liabilities right now for protection agreements. It's a little less than a billion but it's close enough to a billion.

And so the question becomes well we took on the responsibility for that in this transaction. The present value of discharging the obligations is somewhere in the neighborhood of 400 to \$430 million.

However you view it, we are taking on a substantial obligation. If

1 PROCEEDINGS

2 Sears liquidates, that's a billion
3 dollar claim. It's a billion dollar
4 claim because everybody who brought
5 those protection agreements will no
6 longer have protection and have a
7 billion dollars worth of claims
8 against Sears. The fact they can be
9 serviced for \$430 million is
10 irrelevant because no one is there to
11 services it. So we are taking on the
12 obligation of a billion. Yes, it
13 will cost us 430 to service it. But
14 we are taking off the liquidation
15 balance sheet of the debtors
16 approximately a billion dollars of
17 liabilities.

18 There are several other instances
19 where the bid was improved
20 substantially during that period of
21 time, all of which accrues to the
22 benefit of the -- for credit with
23 respect to the nonencumbered assets.

24 Also with respect to the
25 nonencumbered assets, your Honor,

1 PROCEEDINGS

2 there's an issue that goes into
3 liquidation, the liquidation analysis
4 I think as your Honor has said, what
5 we're doing is comparing this
6 transaction to the opportunity
7 presented, the less desirable
8 opportunity hopefully of liquidation.

9 And when you look at the
10 liquidation analysis, including the
11 one that was just presented to your
12 Honor by the debtors in their debt,
13 what you're looking at there is the
14 question of the liability with
15 respect to the priority scheme on how
16 obligations flow through.

17 In this circumstance, this
18 transaction that is being proposed to
19 be approved is substantially better
20 than the liquidation alternative and
21 substantially better than the one the
22 debtors have shown you.

23 In your deck, your Honor, I direct
24 you to, this is page 16 of their
25 deck. This is the benefits of the

PROCEEDINGS

sale transaction in an orderly
winddown. And it's got two columns,
the winddown column and the sale
transaction would assume creditor
recoveries under each column.

The first column under winddown is
the liquidation alternative. So
looking at that first category,
administrative and other priority
claims and assumes recovery under
that liquidation scenario of hundred
percent, that's simply incorrect,
your Honor. Because if you go one,
two, three, four, five lines down
there is a line for second lien
507(B) claims and it says 41 percent.

Now the 507(B) claims your Honor
will recall relate to the second lien
facility that has second lien
positions with respect to all of the
collateral securing the first lien
ABL.

There's been a diminution in value
since the filing of the case. The

1 PROCEEDINGS

2 amount of the collateral, value of
3 the collateral as of the petition
4 date versus the amount of the
5 collateral today is substantially
6 diminished. And that diminution was
7 used to fund the estates and the
8 operations.

9 The 41 percent number is incorrect
10 because the 507(B) claims are senior
11 both by statute and by the order that
12 your Honor ordered to the
13 administrative and other priority
14 claims.

15 So whatever those amounts are, and
16 we understand the debtors made this
17 agreement our point of view which we
18 think is in the neighborhood of 700
19 to 900 million, those 507(B) claims
20 are entitled to recovery before and
21 above the administrative and other
22 priority claims.

23 So what we're talking about here
24 when you flow that through is that
25 the administrative insolvency in a

1 PROCEEDINGS

2 winddown scenario is enormous. And
3 the only way it's not is if you
4 ignore the law and if you ignore the
5 orders that this Court has entered
6 with respect to the 507(B) claims and
7 the diminution of value since the
8 petition date.

9 THE COURT: At least you'd have a
10 fight over it.

11 MR. BROMLEY: We would certainly
12 have a fight about it. And there's a
13 lot of fights we've had, hopefully
14 that's not one of them. But on that
15 one we feel good the statute tells us
16 very clearly and so does the order
17 that your Honor issued.

18 So, your Honor, with respect to
19 the -- going back into the analysis
20 of the release, you know, the
21 subcommittee and Paul, Weiss in the
22 brief made very clear, I won't
23 belabor the point, both equitable
24 subordination and recharacterization
25 are extraordinary remedies. We don't

1 PROCEEDINGS

2 believe that there are facts or
3 circumstances that would give rise to
4 any valid claim.

5 But in the context of trying to
6 make a commercial transaction work
7 here, because of the huge desire that
8 ESL has to try to go forward and this
9 company succeed in the future, we
10 were willing to put the settlement
11 proposal on the table. But it
12 doesn't mean that you shouldn't take
13 into account the fact that the case
14 law is very clear. Those are
15 extraordinary remedies. They do not
16 come -- they do not come across any
17 of our desks in a fully litigated
18 fashion very often and the reason for
19 that is they are incredibly factually
20 intensive and the standards are very
21 high.

22 Your Honor, there's been some
23 criticism made about the conduct of
24 the auction. And we -- and whether
25 it was open and fair and transparent.

1 PROCEEDINGS

2 We were a mere participant and to
3 an extent there was nothing we did to
4 have any role in trying to keep
5 anyone out or anyone in when we
6 showed up at Weil's offices for the
7 auction. We had no idea who would be
8 there or who wouldn't be there or
9 what we were bidding against.

10 We weren't provided with any
11 advance notice of any competing bid.
12 And frankly, as we stand here today
13 have no idea who bid what for
14 anything, notwithstanding demands
15 that we had made for that
16 information.

17 THE COURT: You're going to have
18 to let other people who are objecting
19 have a chance. I don't have how much
20 longer you're going.

21 MR. BROMLEY: I'll be wrapping
22 up, your Honor, sorry. One thing I
23 do want to say, I'm not going to go
24 into any detail refuting the
25 allegations that have been made in

1 PROCEEDINGS

2 the creditors' committees bids. 30
3 or 40 pages of their pleadings were
4 filled with accusations about my
5 client, about actions that may or may
6 not have taken in the prepetition
7 period.

8 We don't view this to be the time
9 or place to be dealing with any of
10 those and we hope that your Honor
11 would be of the same view.

12 To the extent Mr. Qureshi or his
13 colleagues feel a need to get into
14 that and your Honor allows, I want to
15 reserve time to respond to that.

16 Let me see if I have anything
17 else. So I am in light of the issues
18 that have been covered by my
19 colleagues from Weil Gotshal and
20 Paul, Weiss that's all I have for
21 your Honor today. Again, reserving
22 my rights to the extent there's a
23 need. Thank you.

24 THE COURT: Okay. Very well.
25 I'm sorry.

1 PROCEEDINGS

2 MR. SELTZER: Your Honor, I'll
3 only be about two minutes.

4 THE COURT: Okay.

5 MR. SELTZER: Richard Seltzer of
6 Cohen Weiss & Simon for the United
7 Auto Workers, United Steel Workers,
8 Workers United SEIU, DC unions, we're
9 also creditors that represent
10 employees of five distribution soft
11 good centers of the debtors,
12 Pennsylvania, New York and
13 California.

14 One thing I'd say I think it's
15 important listening to this morning
16 that the debtor and the buyer if the
17 sale is approved be in excellent
18 communication with the employees
19 about their status. It sounds like
20 they're going to continue being
21 employees of the debtors for some
22 period of time. Whatever the story
23 is, I think it's important that be
24 communicated to the employees.

25 THE COURT: I agree with you.

PROCEEDINGS

MR. SELTZER: We've been in communication with the debtors and it's our understanding that five locations that we represent people at will be sold and probably three of them will continue operations.

We represent -- the unions I represent, represent hundreds of workers whose jobs are important to them, their families and their communities, and we hope that the debtors and the buyers will have the sense to assume the respective collective bargaining agreements, on the list of agreements that may be assumed because we think that makes sense for labor stability, business stability and equitable agreement.

One of the main goals of Chapter 11 is to preserve jobs. The one case that the creditors' committee cited for sort of the opposite proposition was the *in re After 6* case of Dr. -- of Judge Schoal in Philadelphia and

1 PROCEEDINGS

2 the case actually stands for exactly
3 the opposite.

4 It may be limited in its analysis,
5 but it certainly held that the debtor
6 exercising its business judgment can
7 take into consideration the
8 preservation of jobs in a sale.

9 The point I ultimately rise to
10 make is simple but telling. While
11 the unions we represent do not
12 condone some of the kinds of
13 activities that at least are alleged
14 in the creditors' committees papers
15 and while we do not look at life
16 through rose colored glasses either
17 in the past or the future, at the end
18 of the day the union's members and
19 other employees will either have the
20 opportunity to continue their jobs
21 working for Sears or K-Mart or they
22 will be out of work.

23 In the real world of real working
24 people and real jobs, not the world
25 of armchair experts who sounded to me

1 PROCEEDINGS

2 like were thinking about this
3 alternate universe, these jobs are
4 vital, they're important, they're not
5 easily replaced. There was no other
6 offer to even suggest it, the
7 possibility of maintaining jobs. And
8 so the UAW, USW and Workers United
9 SEIU, while supportive of any efforts
10 to improve the offer, improve the lot
11 of the employees, improve the estate,
12 support the sale. Thank you.

13 THE COURT: Okay. I will hear
14 from your firm, the committee and the
15 other objectors.

16 MR. QURESHI: Thank you, your
17 Honor, Abid Qureshi, Akin Gump, for
18 the committee. May I approach with a
19 short presentation?

20 THE COURT: Sure.

21 MR. QURESHI: Your Honor, before
22 I get into the presentation, there's
23 just a couple of things I'd like to
24 respond to from Mr. Basta's remarks
25 initially. And the first is, and I

1 PROCEEDINGS

2 will say I'm going to approach this a
3 little bit differently, unlike Mr.
4 Basta and Mr. Schrock and Mr.
5 Bromley, I'm not going to testify
6 from the podium which I think your
7 Honor heard a lot of. I'm going to
8 focus instead on the evidence that's
9 in the record.

10 But I do want to respond to the
11 allegation concerning the committee
12 and the committee's decisionmaking
13 process. The suggestion has been
14 made that somehow this committee is
15 dominated by landlords. It's not,
16 your Honor. The committee's
17 membership is two landlords, two
18 trade creditors, one indenture
19 trustee as well as the PBGC.

20 Your Honor, every member of the
21 committee and all of the committee's
22 professionals take their fiduciary
23 duties very seriously and every
24 action the committee has taken in
25 this case has been with the unanimous

1 PROCEEDINGS

2 support of the committee members.

3 Secondly, your Honor, Mr. Basta
4 suggested that the committee has
5 never said let us work the contract I
6 think was the phrase he uses. And
7 frankly, your Honor, given what
8 transpired here, I find that comment
9 really hard to take. Your Honor,
10 there's record evidence that at this
11 auction the committee was not
12 consulted. Yes, it is true --

13 THE COURT: I took what Mr. Basta
14 said with a grain of salt and frankly
15 I don't need to get into
16 deliberations. I'm just evaluating
17 what's in front of me. Motivations
18 are not particularly relevant to me.

19 MR. QURESHI: I agree
20 wholeheartedly with that, your Honor.

21 THE COURT: And I also take -- I
22 mean it sounded facetious but I also
23 take seriously the point that the
24 committee being a total pain in the
25 neck may be the best negotiating

1 PROCEEDINGS

2 strategy. I don't want to get into
3 that.

4 MR. QURESHI: I raise it only,
5 your Honor, because the consultation
6 provision is there so that the
7 committee can be used to improve the
8 deal. And we'd love nothing more
9 than a better deal which we don't
10 have, we have the deal that we have
11 and it's one that we object to.

12 And with that, your Honor, if I
13 could ask the court to turn to the
14 second page of the presentation I
15 handed out. And I want to start with
16 what I think is the fundamental
17 defect in this bid and it relates to
18 the allocation point.

19 As your Honor observed already,
20 the testimony is unanimous from all
21 the witnesses that there was no
22 allocation.

23 Now Mr. Carr in his cross
24 examination made clear why that's an
25 issue. Because he could not explain

1 PROCEEDINGS

2 how the credit bid was being
3 allocated --

4 THE COURT: Let's just go to my
5 question. Is there value here in the
6 unencumbered assets on a reasonable
7 basis in excess of either 3.9 billion
8 or 3.5 billion depending on how you
9 count the rollover of the DIP, the
10 Junior DIP?

11 MR. QURESHI: I think there is,
12 your Honor. If your Honor turns to
13 slide 3. And what I'll try to do
14 here is walk through the numbers.
15 But before I do that, your Honor, we
16 don't accept that the right way to do
17 this is to simply globally take 5.2,
18 deduct 1.3, get 3.9 and it's that
19 simple.

20 The DIP order requires that the
21 ABL only be satisfied by the ABL
22 collateral. This is not an estate
23 that's been substantively
24 consolidated. And so I don't think
25 it's necessarily appropriate to look

1 PROCEEDINGS

2 at it globally on that basis.

3 But, your Honor, let me, if I
4 could, walk through a few of the
5 numbers.

6 So on this --

7 THE COURT: I'm sorry, ABL -- I
8 didn't follow that point. I mean
9 what is happening to the ABL under
10 this deal?

11 MR. QURESHI: So it's being
12 repaid.

13 THE COURT: In cash, not a credit
14 bid.

15 MR. QURESHI: Correct.

16 THE COURT: All right. So let's
17 move on from that point.

18 MR. QURESHI: So, your Honor, if
19 your Honor looks at this chart, and
20 this is a chart that appeared in a
21 slightly different form in our
22 objection, there have been some
23 changes to it based on the testimony
24 and the evidence that's come in, if
25 your Honor looks at the consideration

1 PROCEEDINGS

2 paid column here and what I'd like to
3 focus on first of all is the assumed
4 administrative claim, so the fine
5 numbers, the severance, all those
6 numbers --

7 THE COURT: So this is page what?

8 MR. QURESHI: Page 3 of the
9 presentation.

10 THE COURT: Page 3.

11 MR. QURESHI: And there is a
12 chart there. I'm beginning --

13 THE COURT: I just want to make
14 sure I'm on the right page.

15 MR. QURESHI: I'm on the right
16 side, the consideration paid side of
17 this page. And what's set forth here
18 is a number to be assumed by. And on
19 the top, the Junior DIP we have about
20 \$175 million. Gift card liabilities
21 at \$32 million. That totals 789.

22 Now if your Honor looks a little
23 further down we've included two
24 additional items that we don't think
25 are appropriately in the

1 PROCEEDINGS

2 consideration paid column and I'll
3 explain why. But even if your Honor
4 disagrees with that, we think there's
5 still a shortfall of consideration
6 for the unencumbered assets.

7 Those two items that we disagree
8 with are the PA liabilities,
9 protection agreement liabilities at
10 \$465 million and the additional
11 Junior DIP at \$175 million. And just
12 briefly on those two, your Honor, the
13 assumptions of the Junior DIP, why we
14 in our analysis think that it's only
15 fair to look at half of that as being
16 an assumption, that's because, and
17 this is detailed on the next slide,
18 but, your Honor, the company's own
19 numbers show that the second draw of
20 \$175 million, the online purpose that
21 served was to get these estates from
22 the auction to the closing date
23 essentially.

24 But again --

25 THE COURT: So you're saying

1 PROCEEDINGS

2 that's a 506 (C) claim instead?

3 MR. QURESHI: Your Honor --

4 THE COURT: Understanding
5 Flagstar? Come on, let's be
6 realistic here. I'm at great law now
7 that every DIP loan is subject to 506
8 (C)? Give me a break.

9 MR. QURESHI: So, your Honor --

10 THE COURT: Let's go to the PA
11 liabilities. Have you ever
12 liquidated an insurance company? So
13 how are those claims treated?

14 MR. QURESHI: So, your Honor, the
15 reason that we suggest that the PA
16 liabilities are not appropriate here
17 is because in the winddown scenario
18 there were expressions of interest
19 for the Sears Home Services business
20 and those expressions of interest
21 included --

22 THE COURT: Well get to that
23 point.

24 MR. QURESHI: -- assumption of
25 the liabilities.

1 PROCEEDINGS

2 So, your Honor, let's not take
3 those items out. So consideration
4 paid.

5 THE COURT: No, you're treating
6 them at 465 instead of a billion.

7 MR. QURESHI: That is correct,
8 your Honor. And the reason we do
9 that is again because of the record
10 evidence and the testimony as cited
11 on page 5.

12 THE COURT: That's what they're
13 booked at but as a claim it's a
14 billion dollars. I go back, have you
15 ever liquidated an insurance company?

16 MR. QURESHI: No, your Honor,
17 I've not.

18 THE COURT: All right.

19 MR. QURESHI: And then over on
20 the asset purchase side, your Honor,
21 I want to focus in particular, so
22 there's a low and a high, and the
23 differences are driven, number one,
24 by the real estate valuation. And
25 I'll get to that talking only about

1 PROCEEDINGS

2 the low end numbers. And beyond
3 that, your Honor, it's what we
4 believe to be equity value in
5 Sparrow, in the Sparrow assets and
6 equity value in the assets securing
7 the IGPL loan which are set forth at
8 the bottom of the page and if you
9 total those two up and add it to the
10 other assets that are being
11 purchased, that, your Honor, is where
12 we think we get to the shortfall.

13 And if I can ask the court to turn
14 first next to slide 6. What I want
15 to talk about very briefly is the
16 real estate value to make sure that
17 the court is clear as to in our low
18 end number what constitutes the
19 difference.

20 So there are 555 properties in the
21 debtors unencumbered real estate
22 valuation that the debtors did not
23 value.

24 What Mr. Greenspan did with those
25 properties is he said well let's take

1 PROCEEDINGS

2 a look at them and see if there's any
3 basis to value them. 80 percent of
4 them he agreed he gave zero. The
5 balance he valued at \$126 million.

6 Now two important things with
7 respect to Mr. Greenspan's valuation.
8 One, he did the valuation on a dark
9 basis. So there was no assumption
10 that there would be an operating
11 company that would keep these
12 properties lit with all of the
13 expenses associated with that.

14 Secondly, he deducted from his
15 valuation an estimate of carrying
16 costs for those dark properties to
17 carry them through the length end
18 sale process that this analysis was
19 based on.

20 The second bucket of properties
21 with 402 in it, his valuation 800
22 million as against the debtors at
23 634.

24 So there's that difference is made
25 up of two things. One is, your

1 PROCEEDINGS

2 Honor, the debtors took a 75 percent
3 discount to liquidation value. Mr.
4 Greenspan took a 60 percent discount
5 to liquidation value. For reasons
6 explained in his report which we
7 think are well founded.

8 So in addition, on the debtors'
9 side of that analysis, what the
10 debtors did is their expert gave
11 equal weight in that analysis to
12 nonbinding indications of interest,
13 including those that came in at zero
14 or as your Honor asked Mr. Meghji did
15 that apply equal to a \$500 express of
16 interest and the answer is that it
17 did.

18 THE COURT: Do you dispute that
19 he said the delta there if you didn't
20 include any of that was \$70 million?

21 MR. QURESHI: I believe that's
22 right, your Honor.

23 THE COURT: Do you dispute Mr.
24 Greenspan's testimony that 70 million
25 was just a rounding error so he

1 PROCEEDINGS

2 didn't even include it in his
3 adjustment?

4 MR. QURESHI: I think
5 mathematically the way he expressed
6 his overall range for all of the
7 properties, that's correct.

8 THE COURT: Okay.

9 MR. QURESHI: Now, your Honor, if
10 I could move on.

11 THE COURT: Do you dispute that
12 he ascribed value to leases where the
13 secured interest in the lease
14 exceeded the value of the lease?

15 MR. QURESHI: Your Honor, I don't
16 know the answer to that question.
17 I'll try to get that.

18 Your Honor, if I could ask the
19 court to then turn to slide 8. And
20 this gets to the collateral that
21 secures the Dove and the Sparrow
22 properties.

23 Your Honor will recall I took Mr.
24 Kamalani through this document. There
25 is an appraised value and schedule

1 PROCEEDINGS

2 prepared by Mr. Kamlani of those
3 properties of \$1.65 billion. The
4 term sheet which is also in evidence
5 quite clearly identifies the Dove and
6 the Sparrow collateral as the
7 collateral that secures that loan.

8 If your Honor turns to the next
9 page, we know from the asset purchase
10 agreement that \$544 million of the
11 Dove debt is part of the credit bid
12 here. Mr. Kamlani acknowledged that
13 with that credit bid what ESL was
14 acquiring is the collateral that
15 secured that.

16 So by simple math of subtracting
17 that 54 from the overall 165, the
18 remainder of that value is
19 attributable to the Sparrow
20 properties as acknowledged by Mr.
21 Kamlani.

22 The Sparrow properties have some
23 debt on them that's been credit bid.
24 So you back out that debt and, your
25 Honor, you're left with \$560 million

1 PROCEEDINGS

2 of equity value in Sparrow.

3 And there's no evidence as to how
4 that's being paid for other than by
5 credit bid. Your Honor, similarly,
6 the IPGL loan. If your Honor turns
7 to slide 10. How the IGPL loan is
8 being credit bid as set forth in the
9 asset purchase agreement in the
10 amount of \$231 million.

11 Now, the value of the collateral
12 pledged under that loan exceeds that
13 debt. The debtors, there's two
14 components to that debt, your Honor,
15 one is the IP and the second is the
16 leases. So looking first at the
17 intellectual property, we've
18 excerpted on the page, your Honor, of
19 the winddown recovery from the
20 debtors that shows that the IP in the
21 IGPL loan was valued by Ocean Tomo at
22 \$345 million and with respect to the
23 ground leases that are part of that
24 loan, those were valued by the
25 debtors at \$119 million. That's also

1 PROCEEDINGS

2 excerpted. And that by the way
3 represents a 50 percent discount to
4 the appraised value. So those are
5 conservative values.

6 And Mr. Kamlani, in response to
7 questioning not by me but by Mr.
8 Bromley, confirmed that at the time
9 of that loan, the collateral value
10 exceeded, exceeded the amount being
11 lent and he confirmed, as he did with
12 respect to Sparrow same questions,
13 that he's not aware of any change in
14 those values as of the time that he
15 testified.

16 Your Honor, one more difference
17 between the committees' numbers and
18 the debtors' numbers with respect to
19 the unencumbered value, and that
20 relates to unencumbered collateral
21 where we had, your Honor, back on
22 slide 3 for the other unencumbered
23 accounts receivable a value of 60 to
24 \$80 million, we now have record
25 testimony from Mr. Kamlani that the

1 PROCEEDINGS

2 value of that is significantly
3 higher, \$255 million according to Mr.
4 Kamlani.

5 So, your Honor, the bottom line
6 here is we don't think that there is
7 value being received by these estates
8 for all of the unencumbered assets,
9 and we don't think there's evidence
10 in the record that supports that
11 there is. And on that basis we don't
12 think that the credit bid can be
13 approved.

14 Now, your Honor, if I can move on
15 to the accounts payable chart. And
16 this is addressed on slide 12.

17 If I understand correctly what
18 I've heard from both the debtors and
19 from ESL, we don't have a deal. We
20 don't have a deal because there's a
21 disagreement over what the debtors
22 consider to be, and we agree, a very
23 material term.

24 And, your Honor, an estate that is
25 indisputably being left insolvent

1 PROCEEDINGS

2 today if this transaction closes
3 tomorrow, this estate is simply not
4 in a position to close this
5 transaction and then immediately
6 litigate with Mr. Lampert.

7 And so we do think that this is an
8 issue to the extent your Honor is
9 otherwise prepared to approve this
10 transaction that needs to be resolved
11 and resolved in the debtors' favor
12 before there is a closing. It just
13 makes no sense to close a transaction
14 and begin to litigate.

15 I also think, your Honor --

16 THE COURT: That's exactly what
17 the Second Circuit says I'm supposed
18 to do.

19 MR. QURESHI: We think, your
20 Honor, that certainly in a context
21 here where the estate is
22 administratively insolvent, the
23 company's evidence, not the
24 committee's argument, \$42 million was
25 the amount of the insolvency.

1 PROCEEDINGS

2 And if as I understand the bid and
3 the ask in terms of what ESL is
4 prepared to pay, the amount of
5 administrative insolvency goes up
6 another \$43 million.

7 So while I don't disagree that in
8 other circumstances it might be
9 appropriate to close the transaction
10 and allow that mitigation to happen
11 here, respectfully, your Honor, I
12 don't think that the debtors in the
13 exercise of their sound business
14 judgment can or should do that. Not
15 when there is an alternative in the
16 form of what we have called the
17 alternative sale transaction, the
18 liquidation option, which we think
19 yields a better result to begin with,
20 and not when the estate is simply not
21 going to have the resources to
22 litigate.

23 In addition, your Honor, I think
24 that when one adds what's happening
25 in court today on this provision to

1 PROCEEDINGS

2 all of the other conduct of ESL and
3 of Mr. Lampert that is part of the
4 record, it rises to the level of
5 whether this is a good faith offer
6 under 363.

7 THE COURT: What other comment is
8 part of the record other than
9 litigation claims that you and the
10 special committee are asserting?

11 MR. QURESHI: Your Honor, I'm
12 about to get to it.

13 THE COURT: Okay.

14 MR. QURESHI: So for all of those
15 reasons, your Honor, we don't think
16 it's appropriate, in these
17 circumstances, with an
18 administratively insolvent estate to
19 close on a dispute like this.

20 And unless I misheard the debtors,
21 I don't believe the debtors are
22 prepared to close so long as this is
23 an open issue either.

24 That's how thin the line is in
25 this case between whether this

PROCEEDINGS

transaction makes economic sense or
does not.

Now, your Honor, I think there are
a number of other issues that remain
unresolved. And I will add that we
received overnight more than 600
pages of deal documents, revised sale
order, revised asset purchase
agreement, a transition services
agreement, new releases. Your Honor,
we're simply not in a position,
despite literally having the entire
team up all night, to respond in a
detailed way to very dense documents
that have very material terms in
them.

And yet despite that flood of
overnight documents, as I understand
it, there is still material things
that frankly I'm not sure are
resolved.

503(b)(9) claims, for example.

THE COURT: Have you read the
order? Has anyone on your team read

1 PROCEEDINGS

2 the order?

3 MR. QURESHI: We have, yes, your
4 Honor.

5 THE COURT: What about the
6 representations about the transition
7 services agreement?

8 MR. QURESHI: Your Honor, we are
9 concerned about the mechanics that
10 are going to be in place to deal post
11 closing with 503(b)(9) to ensure that
12 to the extent there's risk there,
13 that is risk that is borne by ESL as
14 the buyer.

15 THE COURT: How concerned are
16 you? Did you raise the issue ever
17 until I raised it yesterday in light
18 of your cross examination that killed
19 the deal?

20 MR. QURESHI: Your Honor, we have
21 had numerous conversations with the
22 debtors.

23 THE COURT: No, no. Did you
24 propose a specific change?

25 MR. QURESHI: Not prior to last

1 PROCEEDINGS

2 night, your Honor.

3 THE COURT: Okay. Why don't you
4 propose one now so I can hear it.

5 MR. QURESHI: Again, your Honor,
6 not having had the time to go through
7 all --

8 THE COURT: You haven't thought
9 about it. It was enough to cross
10 examine someone about it, to raise
11 the issue in my mind. So I raised it
12 immediately. But you're so concerned
13 about these people that you haven't
14 made one proposal.

15 MR. QURESHI: Your Honor --

16 THE COURT: Maybe the two vendors
17 on your committee might think about
18 that.

19 MR. QURESHI: Your Honor --

20 THE COURT: I wasn't going to
21 speculate, but I do now have a record
22 on one big issue as far as your
23 committee's operation.

24 MR. QURESHI: Your Honor, we have
25 --

1 PROCEEDINGS

2 THE COURT: So make the proposal
3 that you say should fix it.

4 MR. QURESHI: We have made clear,
5 your Honor, that the 503(b)(9)
6 provisions, the reconciliation of
7 those claims needs to happen in a way
8 so that the debtor is able to
9 reconcile those liabilities without
10 bearing the risk. That the risk of
11 that should be borne by ESL.

12 THE COURT: But ESL is picking it
13 up. The debtor is liquidating it and
14 it's within the budget that's part of
15 the calculation of the going forward
16 costs. Unless you dispute that.

17 MR. QURESHI: Your Honor, it's
18 not that we dispute it. It's that we
19 haven't been shown the details.

20 THE COURT: It's a claim
21 objection process.

22 MR. QURESHI: Your Honor, also
23 with respect to to the Cyrus release,
24 we just don't understand why a Cyrus
25 release should be approved.

1 PROCEEDINGS

2 First of all, Cyrus does not need
3 a release in order to credit bid.
4 Cyrus consent to a credit bid isn't
5 even required. ESL can and has
6 directed the indenture trustee to
7 credit bid those claims.

8 And secondly, our understanding of
9 the reason I think that the asset
10 purchase agreement as originally
11 filed did not have a release for
12 Cyrus, is that ESL had obtained the
13 financing commitments to satisfy the
14 Junior DIP and that he did that
15 without the need for any release from
16 Cyrus.

17 And so the auction record was
18 clear on that point. And then all of
19 a sudden Cyrus shows up and says we
20 want a release and by the way we're
21 not prepared to pay for it.

22 THE COURT: Well, they rollover
23 the DIP.

24 MR. QURESHI: Again, your Honor,
25 the estate isn't getting anything for

1 PROCEEDINGS

2 that.

3 THE COURT: The DIP is rolled
4 over, it paid for in cash. How much
5 is that Junior DIP?

6 MR. QURESHI: \$300 million.

7 THE COURT: And what would happen
8 if it wasn't rolled over to your
9 administrative claims analysis and
10 your professed concern about
11 administrative insolvency?

12 MR. QURESHI: The concern is not
13 professed, your Honor.

14 THE COURT: Well what would
15 happen to that amount? What would
16 happen to that amount? Would it get
17 paid or not? Would it have to get
18 paid as a priority administrative
19 expense?

20 MR. QURESHI: My understanding,
21 your Honor, is it would have been
22 paid by the financing commitments
23 that ESL had in place.

24 THE COURT: Today, today, the
25 Second Circuit in FNN says that the

1 PROCEEDINGS

2 bankruptcy court has a difficult
3 balancing act in dealing with these
4 decisions in real time. So today,
5 what would happen to that \$335
6 million if you go into a winddown?

7 MR. QURESHI: Today it would be
8 an administrative claim, of course.

9 THE COURT: And instead it's
10 being rolled over and you don't think
11 there's any value to the debtor in
12 that.

13 MR. QURESHI: Your Honor, we are
14 looking at it from the perspective of
15 if the transaction closes.

16 THE COURT: Past tense, because
17 that's what litigators do. They like
18 to litigate things that happen in the
19 past but that's not what bankruptcy
20 lawyers and bankruptcy judges do.
21 They have to look at transactions
22 that are supposed to happen in the
23 future.

24 MR. QURESHI: And when the ESL
25 bid was selected as the highest bid

1 PROCEEDINGS

2 at the auction, ESL had committed
3 financing in place to satisfy the
4 Junior DIP. And they had that
5 financing in place without the need
6 for a release from Cyrus.

7 THE COURT: And now they don't.

8 MR. QURESHI: And now they don't.
9 They changed the deal.

10 THE COURT: So we should just
11 pull the plug.

12 MR. QURESHI: No, we shouldn't
13 pull the plug. We should say to
14 Cyrus go forward but without a
15 release or we should say --

16 THE COURT: I said that last
17 night. I don't know if you did or
18 your partner did. I did and they
19 carved out what seemed to be the real
20 concern which is something beyond the
21 release that ESL was getting. So
22 let's move on.

23 MR. QURESHI: Very well, your
24 Honor.

25 THE COURT: Basically so far I'm

1 PROCEEDINGS

2 finding all of this highly
3 pretextual.

4 MR. QURESHI: I will nonetheless
5 continue to make the record if I may,
6 your Honor.

7 THE COURT: Yes, I know it's hard
8 for you but I know you should go
9 ahead and do that.

10 MR. QURESHI: Your Honor, the
11 transition services agreement, again,
12 one of the documents that we received
13 overnight, and your Honor these are
14 not documents about which we are
15 consulted before we get them, these
16 are not documents about which our
17 input is sought before we receive
18 them.

19 THE COURT: Let me tell you the
20 way I look at the transition services
21 agreement. I agree with you
22 completely on that point. But I have
23 a record here which is that this
24 agreement is more than neutral for
25 the debtor. That the debtor actually

1 PROCEEDINGS

2 does better under this agreement than
3 if they were just compensating each
4 other for their fair value of the
5 services. If that's not true, that's
6 not what I approved. That's what I'm
7 approving, what I just said and what
8 the record says.

9 MR. QURESHI: Your Honor, I
10 didn't think there was any evidence
11 about the TSA.

12 THE COURT: There were
13 representations by both sides as to
14 what it contains and it's bottom
15 line.

16 MR. QURESHI: Your Honor, let me
17 move on to another area that I have
18 no doubt the court will disagree
19 with.

20 THE COURT: Okay.

21 MR. QURESHI: But I will again
22 make the argument nonetheless.

23 We do think that ESL in a number
24 of ways acted inappropriately in the
25 auction process and acted in a way

1 PROCEEDINGS

2 that we think influenced the outcome.

3 Let me go through a number of the
4 ways in which we think that happened.

5 First of all, we introduced into
6 evidence an email from Mr. Transier
7 which we found somewhat odd that an
8 independent director put in place in
9 a role designed to investigate Mr.

10 Lampert would, at the very outset of
11 that process, send him an email with
12 the subject line very impressed,
13 followed by a request from Mr.
14 Lampert that they meet in person.

15 And then we get into the auction
16 process itself when these independent
17 directors, Mr. Transier and Mr. Carr,
18 are supposed to be assessing ESL's
19 bids and what happens? Threats from
20 Mr. Lampert. You're going to get
21 sued immediately. You should be
22 removed from your role as an
23 independent director. You should be
24 bypassed completely because you
25 didn't approve my bid.

1 PROCEEDINGS

2 THE COURT: The threat you're
3 referring to is the letter, right?

4 MR. QURESHI: Yes, it's on slide
5 21. We've excerpted it there.

6 THE COURT: Were you a party to
7 the chambers conference we've all had
8 on that that was called immediately
9 after that letter?

10 MR. QURESHI: I was, your Honor.

11 THE COURT: So since I ran it, I
12 will for the sake of the record state
13 that I said that letter should be put
14 in a drawer and forgotten about
15 because it had no effect and was
16 half-baked because, among other
17 things, it did not deal with the fact
18 that ESL's bids at that point
19 insisted on a complete release. And
20 there's no doubt in my mind that
21 everyone in that conference
22 understood that that letter was a bad
23 letter. And I believe the record
24 reflects, in terms of the
25 negotiations thereafter, that

1 PROCEEDINGS

2 understanding.

3 And if anyone believed to the
4 contrary, including you and your
5 partners, you could have come to me
6 and said, no, they're still leaning
7 on it and I didn't get that. And you
8 know that I would have reacted
9 immediately if I'd been apprised of
10 that.

11 MR. QURESHI: Neither I nor my
12 partners had a different
13 understanding, your Honor. But that
14 is not what's relevant here. What's
15 relevant here is did it have an
16 impact on the decisionmakers? And
17 for that, your Honor, look at the
18 next slide, slide 22. We have
19 minutes where Mr. Schrock explains
20 that it was describing what the
21 advisors and the management had been
22 doing to get to a deal. It was hard
23 to do amid threats of court action
24 from the primary counterparty, where
25 Mr. Schrock describes in the auction

1 PROCEEDINGS

2 transcript a situation that was very
3 difficult for his subcommittee where
4 an insider and a chairman is
5 threatening litigation with the very
6 party whose bid they're supposed to
7 be evaluating.

8 So from that perspective, your
9 Honor, while we certainly as counsel
10 to the committee view the threats to
11 be empty, that's not what's relevant.
12 What's relevant is the decisionmakers
13 and how did the decisionmakers view
14 it?

15 And that is why we referred to it
16 here.

17 Next, your Honor, the letter from
18 the office of the CEO. And this one,
19 your Honor, is the one that I find
20 most troubling. So subsequent to Mr.
21 Lampert's resignation as the CEO, the
22 office of the CEO was created that
23 consists of three people whose names
24 are here on slide 23.

25 Now, your Honor, this is the

1 PROCEEDINGS

2 senior management team of the company
3 whose job it is to provide guidance
4 and make recommendations to the board
5 of directors on numerous important
6 operational issues and most of all
7 during this time frame, the ESL bid.

8 And yet the very people that are
9 supposed to be doing that were
10 requested by Mr. Lampert to write a
11 letter to the board. They then
12 apparently wrote that letter, sent a
13 draft of it to Mr. Lampert's counsel.
14 And then that letter was sent to the
15 board. And the letter says Mr.
16 Lampert, we support you, and we
17 support your bid. And that's the
18 management team that the board is
19 supposed to take advice from, all
20 engineered by Mr. Lampert. So do we
21 think that had an impact on the
22 decisionmaking process? Yes, we do.
23 Do we think that was inappropriate
24 conduct by Mr. Lampert? Yes, we do.

25 Now, your Honor, moving on to the

1 PROCEEDINGS

2 release. And I am not going to get
3 into the merits of the claims. It's
4 never our intention to do that. I
5 will state simply that we
6 incorporated by reference into our
7 pleading our standing motion in the
8 complaint that was attached thereto.
9 We think the claims are very well
10 founded. We think that that
11 complaint in every respect easily
12 passes a motion to dismiss. We think
13 the claims are more than colored.

14 Why do we think the release and
15 the consideration for the release are
16 woefully insufficient here? Two
17 principal reasons, your Honor.
18 Number one, the claim allowance that
19 was allowed here to allow ESL to
20 credit bid, it's more than was needed
21 to allow them to credit bid.

22 We think that if the claims
23 allowance was limited to the \$1.3
24 billion that is credit bid and the
25 balance of the claims were subject to

PROCEEDINGS

recharacterization and equitable subordination, that would have been a more appropriate balance.

Secondly, your Honor, in light of all of ESL's claims being allowed, what is fundamentally problematic from our perspective with the release, the credit bid and the consideration for those two things, is that with the 502 (D) remedy begun up, the estate is now in the position of having to look to ESL and Mr. Lampert to recover on what the restructuring subcommittee agrees are very valuable claims.

There is no record evidence at all that the subcommittee conducted any diligence to inquire into is it going to be easy or difficult to recover against ESL. Where are ESL's assets? Are they offshore? Are they in trusts? How are Mr. Lampert's assets held?

Those are all potentially

PROCEEDINGS

significant collection issues that the estate is now being put at risk of because the 502 (D) remedy has been given up and has been given up to a greater degree than necessary to allow the credit bid. And that's problematic, particularly on a record where no such diligence was performed.

In addition to that, we know from the testimony of Mr. Kamalani that a very substantial portion of the value of ESL is tied up in Sears. And another significant chunk of the value of ESL is tied up in Seritage. Seritage will be a defendant for a very substantial claim.

And we know that a substantial amount of the value of ESL is Mr. Lampert's personal capital, all tied up in Sears and in Seritage.

Your Honor is aware from the evidence we've presented --

THE COURT: I thought the

1 PROCEEDINGS

2 personal capital was separate from
3 Sears and Seritage.

4 MR. QURESHI: I think the
5 evidence is that of the assets under
6 management by ESL, some very
7 substantial portion of that, I think
8 maybe 70 percent, is Mr. Lampert's
9 personal money.

10 So, your Honor, there is --

11 THE COURT: I understand the
12 remedies point. In terms of the
13 showing that you would have to make,
14 it's basically the same, very close.
15 I mean there's some more discretion
16 that a judge would have under
17 equitable subordination, but it's
18 actually quite close particularly
19 given the other -- the language we
20 walked through earlier.

21 But as far as the remedies issue
22 is concerned, the valuations, either
23 on a liquidation basis -- I mean --
24 the valuations on a winddown basis or
25 the valuations of the deal, show that

1 PROCEEDINGS

2 there's substantial value not subject
3 to liens in the purchased assets.

4 And frankly even 30 percent of the
5 remaining 30 percent of ESL would
6 seem to me to be still a very large
7 amount of money you're talking here.

8 So I understand the issue, that
9 you have to go and collect. But
10 given that it's a public company and
11 given that they are certainly on
12 notice of these claims and that any
13 transfers of assets out after that
14 notice would be, per se, a fraudulent
15 transfer under New York law at least,
16 to me I'm not sure why it is such a
17 big deal to equate a release for
18 credit bidding and claim allowance
19 purposes as a general release, in
20 essence.

21 MR. QURESHI: Your Honor, I think
22 it all comes down to the collection
23 risk on the estate and whether it
24 makes sense to take that collection
25 risk when a much more certain remedy

1 PROCEEDINGS

2 is at hand in the form of 502 (B) and
3 while that could have been achieved
4 while still allowing a credit bid.

5 THE COURT: Well except at that
6 point you're collecting from the
7 proceeds of a liquidation of the real
8 estate assets and GOB sales for a
9 relatively short time and fighting
10 with ESL and Cyrus over 507(B), which
11 is a super priority, and 506 (C).

12 So, you know, it's not like you
13 can snap your fingers and bring in
14 the money.

15 MR. QURESHI: Your Honor, let me
16 move on to --

17 THE COURT: I mean, no, I'm not
18 -- that's not rhetorical statement.
19 Am I missing something on that?
20 Because that's how I've been looking
21 at it.

22 MR. QURESHI: No. Look, your
23 Honor, I think that when we assess
24 the reasonableness of the deal that
25 was struck and we weigh the value of

1 PROCEEDINGS

2 the claims on the one hand with the
3 consideration that was received on
4 the other hand, and there was
5 testimony from Mr. Basta about what
6 that consideration was, it doesn't
7 line up at all with what the
8 witnesses said, but that's a
9 different story.

10 THE COURT: But again, it's a
11 consideration for a limited release
12 on remedies.

13 MR. QURESHI: Yes.

14 THE COURT: And, you know, 35
15 million in cash plus a cap on
16 recoveries from certain -- which are
17 effectively going to be the only
18 remaining assets, in return for a
19 limitation on remedies as opposed to
20 bring claims and to go after at least
21 what appear to be substantial assets,
22 seems to me to be a pretty fair deal.

23 MR. QURESHI: Your Honor, the
24 other concern that we have and it
25 continues relating to collection risk

1 PROCEEDINGS

2 is very strong doubts about what's
3 going to happen with the new Sears
4 after this transaction should close.
5 And in particular, your Honor, I'm
6 referring to \$930 million of budgeted
7 for asset sales in three years. That
8 is a very substantial chunk of the
9 value here that's going to get sold.
10 And where those proceeds are going to
11 go we obviously don't know. Whether
12 those assets are going to as they
13 have been in the past get spun off to
14 some other entity that ESL and Mr.
15 Lampert has an interest in, whether
16 that pattern is going to continue we
17 don't know.

18 What we do know is there's a plan
19 in place for very material ongoing
20 selling of assets. And that's a
21 point I'm going to come back to when
22 I talk about jobs.

23 THE COURT: That's fair. On the
24 other hand, I would hope you would be
25 able to progress your litigation

1 PROCEEDINGS

2 faster than three years. I know you
3 would.

4 MR. QURESHI: We certainly intend
5 to try to progress it as fast as
6 possible but we also know, your
7 Honor, because it happened last week
8 we got a liquidity forecast that said
9 \$200 million of real estate sales in
10 2019 and then it was changed, now
11 it's 250.

12 THE COURT: I understand. I
13 understand.

14 MR. QURESHI: How fast that's
15 going to change particularly once
16 ESL's decisions in that respect are
17 no longer subject to bankruptcy court
18 review, we shall see.

19 Your Honor, if I can turn to slide
20 27 and I want to talk briefly about
21 from the committee's perspective why
22 we view the alternative to a sale to
23 ESL to be superior. And I will come
24 back to the employee point, your
25 Honor, after I walk through the

1 PROCEEDINGS

2 numbers.

3 So on this chart, your Honor, what
4 shows first of all is the
5 administrative insolvency.

6 But I also want to make the point
7 here, and it was a point made by Mr.
8 Meghji. Who is the principal
9 beneficiary of the going concern
10 transaction? And I'm going to come
11 back to the employees and the vendors
12 and all of that. The principal
13 beneficiary of the going concern
14 transaction is ESL.

15 THE COURT: I guess that has some
16 appeal to people who don't understand
17 bankruptcy law. But anyone who has
18 read the RadLax decision and 363 (K)
19 knows how much is left unstated in
20 that statement. Right? I mean the
21 reason they are the principal
22 beneficiary is because they are being
23 allowed to credit bid. And we just
24 talked about I think a pretty nuanced
25 evaluation of that settlement which

1 PROCEEDINGS

2 preserved claims against them.

3 So, you know, it's true they're
4 the beneficiary in the sense that
5 they're being allowed to exercise a
6 right that the Supreme Court said
7 they have unless the bankruptcy court
8 says they don't for cause and that's
9 what the settlement is about.

10 MR. QURESHI: Part and parcel,
11 your Honor, of what we think is going
12 to happen postclose and whether
13 postclose this enterprise is likely
14 to survive as a going concern and
15 whether as a result of that all of
16 the creditors that would benefit are
17 in fact ever going to realize that
18 benefit and whether in fact all of
19 those creditors might actually be
20 better off if we look at an
21 alternative scenario.

22 THE COURT: Okay, that's a point
23 but go ahead.

24 MR. QURESHI: On the alternative
25 scenario, your Honor, if your Honor

PROCEEDINGS

turns to slide 28. And what slide 28 is is an excerpt from Mr. Burian's declaration. And I just want to highlight to your Honor what -- how few things he's moved in order to demonstrate that credit recoveries are actually better in the alternative, in the alternative scenario.

So for unsecured creditors first of all, there is an issue and it's described in Mr. Burian's declaration in some detail but around the allocation of administrative claims and the extent to which those administrative claims for unencumbered assets versus the ABL collateral, we don't think that the way the debtors have proposed in their analysis of the winddown scenario to burden the unsecured claims is appropriate.

THE COURT: Is that a 506 (C) point?

1 PROCEEDINGS

2 MR. QURESHI: Yes. And --

3 THE COURT: So how are you going
4 to get around the Second Circuit law
5 on that point and the law in the
6 other circuits including Domistyle,
7 that you would have to show primary
8 and direct benefit?

9 MR. QURESHI: Well, I mean, your
10 Honor, we think when the ABL
11 collateral --

12 THE COURT: Including when you
13 have a 506 (C) waiver and a DIP
14 agreement.

15 MR. QURESHI: There is no waiver
16 for the second lien, your Honor.

17 THE COURT: I'm talking about the
18 first lien. So you're not really
19 talking about the ABL, you're talking
20 about the second lien.

21 MR. QURESHI: I'm sorry, that is
22 correct. The number here that is
23 moved that is boxed in Mr. Burian's
24 analysis, it's the second lien.

25 THE COURT: Okay. And so you

1 PROCEEDINGS

2 would have to establish,
3 notwithstanding Flagstar and
4 Domistyle and all the other cases
5 dealing with 506 (C), that this is as
6 simple a case as selling a piece of
7 real estate for anything that has a
8 mortgage on the property.

9 MR. QURESHI: Your Honor, I have
10 no doubt there would be litigation
11 around the issue. But we do think
12 there is an argument that a
13 reallocation --

14 THE COURT: It's an argument. I
15 understand the argument. I also went
16 through that experience with a very
17 inexperienced secured lender group in
18 a case last year where they didn't
19 agree to carveouts and the like or to
20 fund the case even though they wanted
21 the case funded. It was -- you may
22 well be better lawyers than their
23 lawyers, although their lawyers were
24 pretty good for the debtors' side.
25 It's not an easy case to win. And it

1 PROCEEDINGS

2 was settled with major haircuts to
3 the professionals and the other
4 administrative expense because the
5 standard is a high one to meet. The
6 Second Circuit has set a high
7 standard and that's been followed by
8 the other courts.

9 MR. QURESHI: Your Honor, the
10 other significant driver --

11 THE COURT: I didn't see anything
12 on that issue, by the way. It's
13 assumed by Mr. Burian who I know is a
14 lawyer but he hasn't been a lawyer
15 for a long time.

16 MR. QURESHI: Your Honor, the
17 other issue and we do address it in
18 our brief is the second lien 507(B)
19 claim Mr. Bromley mentioned briefly
20 so I won't spend any more time there.

21 THE COURT: You're giving no
22 value to that, right?

23 MR. QURESHI: In this analysis we
24 are not.

25 THE COURT: No, okay.

1 PROCEEDINGS

2 MR. QURESHI: Your Honor, if I
3 could then move on --

4 THE COURT: Is that because the
5 value of the collateral declined or
6 didn't decline? I mean didn't
7 decline during the case? Is there
8 evidence in the record to show that
9 the value of the collateral didn't
10 decline?

11 MR. QURESHI: Your Honor, again
12 --

13 THE COURT: I don't think there's
14 evidence to show it did decline. To
15 say it didn't is kind of a stretch
16 here given the amounts that at least
17 the debtors have said that they are
18 operating at a deficit at times.

19 MR. QURESHI: Your Honor, if I
20 could turn to very briefly the
21 business plan.

22 And this starts on slide 30. And,
23 your Honor, our point with the
24 business plan is simply this. That
25 history has to be a guide here and it

1 PROCEEDINGS

2 has to be a guide in circumstances
3 where you have the same management
4 team in place that put together the
5 ESL business plan. That's what the
6 evidence shows. Obviously the same
7 ownership structure in terms of Mr.
8 Lampert being at the helm of the
9 go-forward business.

10 And when your Honor looks at the
11 historical results, frankly, your
12 Honor, I've never seen anything like
13 it. Magnitudes of misses so huge,
14 and yet year after year those misses
15 having no impact on the projections
16 for the next year, as though history
17 didn't occur.

18 And when we look at the go-forward
19 plan, and yes, Mr. Kniffen did not
20 testify here and it's curious that
21 Mr. Bromley expresses so much
22 confidence in his ability to have him
23 excluded by way of a Daubert
24 challenge and yet nobody wanted to
25 cross examine him.

1 PROCEEDINGS

2 THE COURT: I did read the
3 deposition. I mean it's true there's
4 no challenge. I guess he's been
5 accepted as an expert, right?

6 MR. QURESHI: He has.

7 THE COURT: But he also is clear
8 that he's never written anything on
9 this issue, there's no peer review of
10 his analysis or methodology of his
11 analysis. So I took it for what it
12 was worth. And I understand your
13 point about his projections. The
14 debtors are asking me to accept the
15 projections for basically 2018. I
16 mean the performance, the real
17 performance in 2018 to counteract all
18 of the years of missed projections.
19 And I understand that point.

20 MR. QURESHI: Your Honor, what
21 Mr. Kniffen does have is 30 years of
22 experience as a senior executive.

23 THE COURT: Although he also says
24 retail has changed a lot since the
25 last time he actually worked for

PROCEEDINGS

retail.

MR. QURESHI: Yes, but since --

THE COURT: I think 2005, right.

MR. QURESHI: 2005 I believe since he left the May department stores, that's right, which is where he was, but he's obviously remained in the business since then.

THE COURT: I was trying to think back what sort of computer I had in 2005. It's totally different world today.

MR. QURESHI: And it's a world he's still involved in, your Honor.

THE COURT: Sort of.

MR. QURESHI: On a day-to-day basis. Your Honor says sort of. I think his deposition is clear he's a full time consultant in the retail industry.

THE COURT: I know, he walks through malls, I understand. I read his deposition. I didn't -- look, this is an inexact exercise to begin

1 PROCEEDINGS

2 with. And frankly there was one
3 element of the exercise that just was
4 flat out wrong, I think, and you
5 should respond to that, which is the
6 occupancy point.

7 MR. QURESHI: Your Honor, on the
8 occupancy point, he is, as I
9 understand it, pulling numbers from
10 the debtors' filings. And I don't
11 think that has a material impact on
12 his observations. I think the key
13 observations that he makes, your
14 Honor, are that if you look at the
15 excerpt from his report that we have
16 on page 30, the type of growth that
17 is projected. At the same time that
18 SG&A is going to get slashed by \$600
19 million a year, something this
20 company has been trying to
21 unsuccessfully do for years, that
22 EBITDA growth is going to continue.
23 That margin growth is going to
24 continue. It's something that he
25 says it's just unprecedented to see

1 PROCEEDINGS

2 that kind of turnaround.

3 And when you peel the onion back
4 the next layer, your Honor, you look
5 at the business plan and you ask
6 yourself well what's driving it?
7 Well the key is apparently Shop Your
8 Way. That's what we heard from Mr.
9 Kamlani. He went on at length in his
10 deposition about it. Mr. Lampert
11 went on even longer in his interview
12 about it.

13 And yet the initiatives that are
14 going to be the source of all this
15 revenue are the same initiatives that
16 are in the business plans from years
17 past. Nothing's changed.

18 And in addition to that, your
19 Honor, we have some contradictory
20 testimony and Mr. Kamlani says well
21 the ecosystem is how he referred to
22 it is important. And the bigger the
23 ecosystem the better for Shop Your
24 Way.

25 And Mr. Riecker says smaller

1 PROCEEDINGS

2 footprint is better because we're
3 getting rid of all the EBITDA
4 negative stores and we can shrink our
5 SG&A.

6 THE COURT: How do the parties --
7 I want to make sure I understand the
8 defined term ecosystem. I understood
9 it to mean the fact that Sears has
10 warranties, service people, that sort
11 of stuff, the inner realm. That's
12 how I interpreted it. But I don't
13 know. Is that how the parties are --
14 like I said how he's using it?

15 MR. QURESHI: I believe that that
16 is how Mr. Kamlani is using it and
17 when he uses it --

18 THE COURT: Those aren't going
19 away.

20 MR. QURESHI: No, but when he
21 uses it in the context of Shop Your
22 Way, I believe, and there's a long
23 back and forth between Mr. Kamlani
24 and I in his deposition about this,
25 that what he is also talking about is

1 PROCEEDINGS

2 that the value of Shop Your Way is
3 dependent on attracting partners,
4 outside partners.

5 THE COURT: I understand.

6 MR. QURESHI: And that's easier
7 to do when you have a bigger
8 footprint.

9 THE COURT: Or maybe more, more
10 profitable stores where people like
11 to shop more. I don't know. I agree
12 with you. Unfortunately in today's
13 world where there is a company that
14 used to print textbooks or a company
15 that sells plus sized clothes, that's
16 changed everything. And frankly any
17 projection is more in doubt than a
18 normal projection that you would have
19 had fifteen years ago or ten years
20 ago because of that. It's very hard
21 to predict. I agree with all of
22 that, definitely.

23 MR. QURESHI: And in an industry
24 when it's very hard to predict hockey
25 stick like projections which is what

1 PROCEEDINGS

2 these look like are even more
3 unreasonable than in an industry
4 where that's not the case, where the
5 history of the company is wild misses
6 year after year, and it's the same
7 company going forward with the same
8 management team.

9 THE COURT: That's the part I'm
10 not so sure about, the same company
11 going forward. I understand the
12 management team does seem to me that
13 they had a huge drag with the size of
14 the company and the debt load,
15 whether that's enough or not.

16 MR. QURESHI: So, your Honor, let
17 me go on. As I said I would to
18 address the issue of jobs. And the
19 first thing I'm going to do is defend
20 the committee and defend the
21 committee's advisors because, your
22 Honor, it's just not the case that we
23 have ignored the interests of
24 employees, that we don't care about
25 the interests of employees, that Mr.

1 PROCEEDINGS

2 Burian doesn't care about the
3 interests of employees or that that
4 wasn't something that wasn't
5 considered in connection with all the
6 analysis we did. This committee and
7 every member on it owe fiduciary
8 duties and those duties have been
9 taken very seriously. Everybody has
10 acted faithful to those duties. And,
11 your Honor, the bottom line is there
12 are situations in bankruptcy where
13 liquidation can be the better option.
14 It's never pleasant. It's not
15 something anybody involved in a
16 bankruptcy case wishes for. But
17 sometimes it's the better result.
18 And here we believe that it is the
19 better result for all of the reasons
20 we've been talking about.

21 But what I want to make clear is
22 that this has been presented, your
23 Honor, as a decision between 45,000
24 jobs on the one hand and zero on the
25 other. And that's also not right.

1 PROCEEDINGS

2 Because in the alternative scenario
3 there are standalone pieces of this
4 business, like Sears Home Services,
5 like Innovel, like Parts Direct, that
6 in the aggregate employ over 10,000
7 people. And those are jobs that
8 would be preserved.

9 THE COURT: What sort of
10 decisions were made on those?

11 MR. QURESHI: So, your Honor,
12 it's detailed in Mr. Burian's report.
13 And if your Honor goes back to slide
14 3 of the deck, the values that are on
15 the asset purchase side there for
16 Sears Home Services and the repair
17 business and SHIP business, that
18 reflects indications of interest or
19 bids that were put in as part of the
20 sale process.

21 Because of how that process went,
22 your Honor, those never were
23 progressed to definitive bids. But
24 those were all as I understand it
25 indications of interest where the

1 PROCEEDINGS

2 intent was that the business would
3 continue.

4 THE COURT: Would those
5 indications of interest assume that
6 Sears would continue?

7 MR. QURESHI: Your Honor, I don't
8 think so. With respect to I believe
9 it was the Sears Home Services
10 business, I think there was one bid
11 that originally did contemplate and
12 had some contingency in it about
13 Sears stores and then there was a
14 revision of that or at least
15 discussions concerning that where
16 that was then no longer the case at
17 least with respect to one of those
18 parties.

19 So it's not a case of 45,000
20 versus zero.

21 And the other thing that I think
22 is significant, your Honor, and it's
23 part of the record, look at slide 31.
24 Slide 31 is a history of jobs.

25 THE COURT: I don't doubt it's

1 PROCEEDINGS

2 gone down. There's no doubt about
3 that.

4 MR. QURESHI: And more to the
5 point, your Honor, so it's the
6 trajectory under Mr. Lampert's
7 leadership. Not that I'm suggesting
8 that the Internet didn't happen. But
9 with all the substantial asset
10 spinoffs that obviously had a very
11 significant impact on employment.

12 In addition, your Honor, I'll come
13 back to what we've excerpted on slide
14 32, which is the asset sales.

15 I mean, your Honor, when Mr.
16 Burian talks about the process and
17 the process as far as the sale
18 process and how rushed it was, let's
19 be clear Mr. Burian is not
20 criticizing Lazard, the debtors'
21 investment bankers. It's really a
22 criticism of Mr. Lampert. Lazard was
23 brought in basically at the filing.
24 There was no time to prepare a proper
25 sale process. And frankly we think

PROCEEDINGS

it's because that's exactly how Mr.
Lampert wanted it.

He set up a process where there
was no alternative but for ESL to be
standing alone as the only party that
could possibly put forward a going
concern bid in the very limited time
that was left. It was a chaotic
filing at the most important time of
year for a retailer.

And looking at that from the
outside it made no sense.

And that was preceded by a long
period of time where in effect --

THE COURT: Is there anything in
the record to indicate that any other
going concern party said, for
example, give me a little more time,
I'm happy to make a bid, etc.?

MR. QURESHI: Your Honor, there
are a number of statements in Mr.
Burian's declaration that go to
conversations that he had with
bidders where, as your Honor just put

1 PROCEEDINGS

2 it, those statements were not
3 expressly made.

4 THE COURT: I'm talking about a
5 going concern bidder.

6 MR. QURESHI: For the entirety of
7 the business, no, your Honor.

8 THE COURT: So we're really
9 talking about the segments.

10 MR. QURESHI: We're really
11 talking about the segments. But
12 again this entire process was in our
13 view set up to fail. Not Lazard's
14 fault. They did the best they could
15 in the very limited amount of time
16 they had.

17 THE COURT: Did anyone ask to
18 extend the process in any way or
19 raise those concerns? I don't
20 remember hearing from Mr. Burian
21 about those concerns. And you know
22 how active I am when anyone does
23 raise a concern, for example, when I
24 got a call from one of the real
25 estate's counsel, I think I responded

1 PROCEEDINGS

2 to the debtors and him within five
3 minutes of getting the email. Was
4 that concern ever raised to me during
5 the sale process?

6 MR. QURESHI: Your Honor, the
7 concern was raised by this committee
8 from day one.

9 THE COURT: To me.

10 MR. QURESHI: Which concern
11 specifically, your Honor.

12 THE COURT: Articulated in Mr.
13 Burian's declaration about
14 information not being available,
15 people wanting to bid and not
16 knowing, the requests being denied,
17 etc., etc., etc.

18 MR. QURESHI: Your Honor, we
19 raised those concerns with the
20 debtors. We did not file a motion.
21 We did not seek relief from the
22 court.

23 THE COURT: Or even request a
24 chambers conference to discuss it.

25 MR. QURESHI: We did not, your

1 PROCEEDINGS

2 Honor.

3 THE COURT: Might it be because
4 you didn't want a going concern sale
5 in the first place?

6 MR. QURESHI: Your Honor, we made
7 clear from the very early days of
8 this case that we were very concerned
9 by the administrative burn, millions
10 of dollars a day.

11 THE COURT: So it would have to
12 be a fast process anyway.

13 MR. QURESHI: Given the way it
14 was set up by Mr. Lampert it
15 absolutely would have to be a fast
16 process. And unfortunately that's
17 one of the reasons and one of the
18 dynamics why we think in this
19 circumstance the alternative would be
20 better. It's just the reality of the
21 situation, your Honor.

22 Now, had -- and certainly in the
23 claims that will be brought against
24 Mr. Lampert and that will be brought
25 against ESL, these facts will all

1 PROCEEDINGS

2 come to light. And I'm not here to
3 litigate those now. But we do think
4 and we think there's evidence to
5 support that Mr. Lampert knew exactly
6 what he was doing when he elected not
7 to commence a reorganization for
8 Sears years earlier than he did, with
9 advice from investment bankers he
10 retained at the time telling him of
11 exactly the risk of what would happen
12 if he didn't do it, which is what
13 would happen here. Telling him
14 specifically that with retailers
15 there's a high risk of liquidation.

16 THE COURT: I'm sorry. I guess
17 -- you know I usually don't pay a
18 whole lot of attention to the buyer
19 when they stand up in support of a
20 sale. But there was to me some
21 cogency to Mr. Bromley's argument
22 that if ESL really wanted to take the
23 assets, it would -- it would actually
24 cause a liquidation. And it could
25 cherrypick the assets it wanted.

1 PROCEEDINGS

2 MR. QURESHI: I think, your
3 Honor, that that for ESL is a far
4 inferior result than being able to
5 credit bid all of their claims.

6 And by the way, Mr. Bromley --

7 THE COURT: You could credit bid
8 on just the assets you want.

9 MR. QURESHI: And Mr. Bromley
10 also --

11 THE COURT: That you have leads
12 on.

13 MR. QURESHI: And Mr. Bromley
14 also says the claims against his
15 client have no merit.

16 THE COURT: That's a separate
17 issue. I'm accepting that they have
18 merit because I have two independent
19 parties with well staffed law firms
20 telling me so. That will have to be
21 sorted out in the future.

22 MR. QURESHI: What we see, your
23 Honor, in the business plan and in
24 particular in the plans for asset
25 sales under that business plan, is a

1 PROCEEDINGS

2 continuation postclose of what
3 happened prepetition which is a
4 continuing selling of assets. And,
5 your Honor, Mr. Kamlani and ESL I
6 think are very careful in saying,
7 look, we're making offers of
8 employment to these 45,000 people.

9 There is no obligation to employ
10 them for more than a day. He's clear
11 that he doesn't know or at least
12 hasn't yet decided exactly what's
13 going to be sold and what the
14 employee reductions are going to be
15 as a result of that.

16 But it doesn't take much, your
17 Honor, to figure out that at \$930
18 million worth of asset sales there's
19 going to be a lot of lit stores in
20 that number that end up getting sold
21 and likely a lot of job losses as a
22 result.

23 So, your Honor, to sum up, the
24 very party that was accused by the
25 restructuring committee, and, your

1 PROCEEDINGS

2 Honor, on slide 3 there's an excerpt
3 from the auction transcript, and this
4 is Mr. Basta speaking, he talks about
5 ESL's abuse of its control and about
6 the transfers of hundreds of millions
7 of dollars of assets and those
8 transfers hurting Sears and its
9 employees, it's rather ironic that
10 that very individual is now presented
11 as a savior for all of these jobs.

12 Your Honor, I had shown Mr. Carr a
13 series of text messages that he was
14 exchanging with his advisors. And he
15 was doing so right around the time
16 ESL bids were being considered. And
17 the one in particular that I focus
18 on, the reason I focus on it is where
19 Mr. Carr says it's close enough.

20 Respectfully, your Honor, a proper
21 analysis here where we have
22 everything that we have going on, an
23 insider, an insider who is not just a
24 regular insider, he's the chairman
25 and the CEO of the company, an

1 PROCEEDINGS

2 insider against whom valuable claims
3 have been alleged, when that same
4 insider who has taken the steps that
5 I've described in terms of his
6 involvement in the auction process,
7 when that's what's going on and a bid
8 by that insider is tabled, close
9 enough doesn't cut it. Whatever the
10 standard is, and we've briefed the
11 issue of whether it should be
12 heightened scrutiny or business
13 judgment, under either standard,
14 under any standard close enough? And
15 we've got cover? Shouldn't cover.

16 THE COURT: Show me that. I'm
17 not sure I understand the close
18 enough. I think you're quoting it
19 out of context.

20 MR. QURESHI: It's the second to
21 last page, your Honor. Page 34. So
22 this is the text message exchange on
23 January the 8th.

24 THE COURT: January 8th?

25 MR. QURESHI: Yes.

1 PROCEEDINGS

2 THE COURT: All right. I will
3 tell you what that is, all right.
4 That's when everyone came into my
5 office and said we don't think we can
6 go any farther. I heard the parties
7 and made the assessment no, you can
8 go farther. And that's what he's
9 referring to when he says close
10 enough for government work. I think
11 he's saying he's not so sure I'm
12 right, but he did then testify that
13 \$800 million was added to the
14 transaction thereafter and the
15 release was limited as we've already
16 discussed. And I think as you have
17 conceded is reasonable. So I think
18 you misquoted that.

19 MR. QURESHI: Well, your Honor,
20 the text right above it where Mr.
21 Carr writes to Mr. Stogsdill says
22 this is good and gives us cover.

23 THE COURT: January 8th, exactly.
24 Blame it on the judge. That's fine.
25 That's what the judge does sometimes.

1 PROCEEDINGS

2 Look, I appreciate, I remember
3 Eastern, Eastern, you know, the judge
4 said this airline should survive, it
5 didn't and it didn't because the
6 person who ran the airline messed it
7 up. I understand those things. I've
8 been around for a while.

9 So but don't misquote someone
10 about their decision based on
11 something that happened seven days
12 before the decision was made and
13 after several rejections of interim
14 offers.

15 MR. QURESHI: Your Honor, I'm
16 certainly not blaming the judge as
17 the court put it by any stretch.

18 THE COURT: That's not the point.
19 I'm saying don't misquote Mr. Carr.

20 MR. QURESHI: I don't think I
21 did.

22 THE COURT: It's totally out of
23 context.

24 MR. QURESHI: I don't believe we
25 are misquoting Mr. Carr.

1 PROCEEDINGS

2 THE COURT: Well I do, I do.

3 He's talking about a specific point
4 when I said keep talking to each
5 other, period. That's all he's
6 talking about. And he was pretty
7 much fed up with Mr. Lampert at that
8 point, as people got fed up with Mr.
9 De Lorenzo 30 years ago.

10 And I believed, and he certainly
11 was certainly within his rights
12 because the judge only sees about
13 five percent of what's going on in a
14 case, but I believe based on the
15 conference that I had with the
16 parties, that there was a basis for a
17 limited period with protection for
18 the estate to keep talking. That's
19 what he's talking about. That's the
20 cover.

21 So I don't fault him for the
22 email. But I do fault you for
23 misquoting it in the context. It's
24 not the approval of the overall deal.
25 It's the approval of an interim step

1 PROCEEDINGS

2 in the deal.

3 MR. QURESHI: Your Honor, I will
4 end with this. I don't think there's
5 a deal to be done today.

6 THE COURT: Okay. So I know
7 there may be other -- I know there's
8 at least one other party that wanted
9 to speak because she was on the
10 phone. Are there other parties that
11 want to address their objections?

12 I'm sorry, my courtroom deputy
13 tells me this oral argument has gone
14 a lot longer than the court
15 originally thought and she tells me
16 that we don't have this room beyond 1
17 o'clock. We have to go into my
18 courtroom.

19 So I think it may make sense,
20 since it's only ten minutes to one
21 and there are about 150 people in
22 this room, that we should break now,
23 set up the call again and then hear
24 the other objectors.

25 Someone has like a two minute

1 PROCEEDINGS

2 update. One minute update. That's
3 fine.

4 MR. HAYNES: Thank you very much,
5 your Honor, for the report, Robert
6 Lee Haynes, Kelly Drye & Warren on
7 behalf of Brookfield Property Site
8 Centers and numerous other landlords.

9 Your Honor, as Mr. Schrock
10 indicated on the first day of the
11 case we have been working a group of
12 landlord counsel on behalf of a
13 significant portion of the landlords
14 to try to work and make sure that the
15 form of order incorporated the
16 concept that all landlord rights
17 would be adjourned and preserved,
18 that designation rights process would
19 fully do that. It's obviously been a
20 moving process.

21 I believe we are there and have
22 been able to work closely with
23 counsel for the debtor and ESL
24 throughout the four or five days now.
25 There were some curve balls thrown at

1 PROCEEDINGS

2 us including a lien on leases and new
3 financing package. I think we've
4 resolved those consistent with your
5 prior decisions in that. We are
6 waiting to hear from counsel for the
7 secured lenders on the exit facility
8 to confirm that. But as far as that
9 goes, your Honor, I believe we're in
10 a place we believe all our rights
11 have been reserved.

12 THE COURT: I did see the
13 blackline of the order that I think
14 did that. I appreciate the
15 confirmation of that.

16 MR. HAYNES: Thank you, your
17 Honor.

18 THE COURT: I'm serious, unless
19 it's like 30 seconds I really need to
20 get the people out of this room
21 because they're going to be having a
22 jury assembly here or something for
23 the district court.

24 I'm going to adjourn for about 10
25 minutes and we'll get you back on the

1 PROCEEDINGS

2 phone, all of you who are on the
3 phone and resume at about five after
4 one.

5 (A recess was taken.)

6 THE COURT: We're back on the
7 record in re Sears Holdings
8 Corporation. Just want to make sure
9 we have court call on, correct? I
10 mean the people on the phone, put it
11 that way.

12 AUDIENCE MEMBER VIA PHONE: Yes,
13 your Honor, we are connected.

14 THE COURT: All right. When we
15 left off I was about to hear the
16 other remaining objections or
17 statements or reservations.

18 MR. ZUMBRO: Good afternoon, your
19 Honor, Paul Zumbro from Cravath
20 Swaine & Moore on behalf of Stanley
21 Black+Decker. Your Honor, we have no
22 objection to the sale itself as Mr.
23 Sharp just reminded we have a
24 discrete issue in the overall context
25 of this hearing but's important to my

PROCEEDINGS

client. Our objection is that docket number 2072. We have an assumption and assignment objection and a cure objection. The cure objection is relatively straightforward. I will address that briefly at the end of my presentation. The assumption assignment objection however is a bit more complex.

That objection concerns the proposal to assume and assign a valuable trademark license without our consent. By way of background, your Honor, my client Stanley Black+Decker purchased the Craftsman brand and the related trademark from Sears in early 2017 for approximately \$900 million. In connection with that transaction SBD licensed back to Sears a license to allow Sears to use the Craftsman mark in the sale of Craftsman branded tools and other Craftsman branded products in Sears retail stores. That trademark

PROCEEDINGS

license agreement was included in the list of initial assigned agreements that the debtors recently filed in connection with the proposed sales.

Your Honor, as I mentioned, we have not consented to that consignment. And unlike a garden variety contract where the bankruptcy code overrides anti-assignment provisions, applicable law here gives a trademark owner clear consent rights.

The starting point, your Honor, in section 365 (C) (1) of the --

THE COURT: Can I just interrupt you. I think I understand the basis for the debtors' objection in response to this. I'm not sure you need to get into all of that because I think the debtor has a more limited objection.

MR. ZUMBRO: More limited response, sir.

THE COURT: Yes.

1 PROCEEDINGS

2 MR. ZUMBRO: I'll hop right to
3 that. It basically comes down to
4 just quickly trademark law is very
5 clear that the trademark owners'
6 consent is required unless there's an
7 express assignment provision in the
8 contract. There is an express
9 assignment provision in the contract,
10 but in our case it's limited to a
11 sale of all or substantially all of
12 the assets.

13 Those are the only circumstances
14 in which the licensee can assign the
15 license. And we understand, your
16 Honor, that the debtors' position is
17 that because all that's left over is
18 being sold to ESL, that satisfies the
19 all or substantially all test. But
20 that's not a correct recitation of
21 New York law. The debtors cite
22 solely an unpublished Chancery Court
23 opinion from Delaware. The actual
24 law in the Second Circuit on this
25 topic is Sharon Steel on the one hand

PROCEEDINGS

and Sharon Steel teaches that if there's been a plan of liquidation or a plan of sales you have to look back to the beginning of the plan and then you compare what the assets were at the beginning of the plan versus what's now proposed to be sold to test whether it's all or substantially all. And then there's another case that's also recent where the Delaware Supreme Court was interpreting New York law and it said very clearly that a sale of all that's left over does not constitute a sale of all or substantially all. So we think it's very clear, your Honor --

THE COURT: I'm sorry. So you're saying those cases stand for the proposition that you look at what point in time to determine whether it's all or substantially all?

MR. ZUMBRO: Your Honor, it's not crystal clear under the law. The

PROCEEDINGS

debtor will say it's not the time of the contract and even if I concede that, if it's at the time of the contract there was 1430 stores at the time, but if I point your Honor to mid 2017 where Sears publicly announced an intention, a plan to liquidate all of its unprofitable stores in a sort of planned event, I think that's an appropriate time to look back to which is mid 2017 when they publicly said they were going to start liquidating their stores.

So there was about 1150 stores at that time versus the 425 that are being proposed to be sold today.

It's like 30 percent. It's nowhere near all or substantially all. If we even looked at the petition date, your Honor, just looked at what's happened during the course of this case we've gone from 687 stores down to 425 stores which are now being proposed to be sold. That's about 60

1 PROCEEDINGS

2 percent, your Honor. That is not all
3 or substantially all under either a
4 common use of the term or what the
5 courts have said all or substantially
6 all means. It's a very high
7 threshold, your Honor.

8 So what we're saying --

9 THE COURT: Well except frankly
10 as I remember it the case law was
11 pretty sparse on this either way. I
12 don't think -- the whole issue is the
13 timing issue when you -- how you
14 define the process of selling all the
15 assets or substantially all the
16 assets.

17 MR. ZUMBRO: I understood --

18 THE COURT: Right now it's just
19 two lawyers talking to me. I don't
20 really have a factual record. I know
21 what happened in this case. I will
22 say that this is a sale of all or
23 substantially all of the assets
24 because it is substantially all of
25 the assets. But I don't know what

1 PROCEEDINGS

2 was done prepetition as far as some
3 sort of formal plan to sell assets.

4 MR. ZUMBRO: I understand, your
5 Honor. But if even if I could just
6 focus the court on what's happened
7 while this case has been under your
8 supervision. Like I said the Liberty
9 Media case which we cited to in our
10 response to the debtors' response
11 says it very clear that purchasing
12 whatever assets are left at the time
13 of the sale, which is exactly what
14 we're doing here, doesn't constitute
15 all or substantially all.

16 THE COURT: Were those
17 substantially all of the assets on
18 the start of the petition date on
19 Liberty Media?

20 MR. ZUMBRO: It wasn't a
21 bankruptcy case. There was a plan in
22 that case where there was a plan over
23 a series of time.

24 THE COURT: This is a different
25 context we are in at this point.

PROCEEDINGS

They were certainly heading toward a sale.

MR. ZUMBRO: Look, your Honor, cutting through it, we think we have a right to determine who our licensee is here, and that's fundamentally what trademark law provides.

THE COURT: I know but the parties can vary that by their agreement.

MR. ZUMBRO: I understand that. But here their agreement was if someone is purchasing Sears, all of Sears, they can continue the license. But this is not Sears. I just heard your Honor during Mr. Qureshi's presentation say it's not clear to the court that this is the same company going forward as it was as Sears. And we agree with that. We have that same concern. It's not clear to us either.

THE COURT: As far as this case is concerned, these are the assets

1 PROCEEDINGS

2 that matter. The rest was GOB sales.

3 I mean that's just selling stuff on
4 the shelves.

5 MR. ZUMBRO: I understand. But
6 our license was very specifically
7 crafted to Sears and to very
8 specifically identify channels of
9 retail trade which were defined as
10 Sears retail stores of a certain
11 type, of a certain size. I think
12 you've heard lots of testimony over
13 the last couple of days. We don't
14 know what Newco is going to be going
15 forward. We don't know what their
16 footprint is going to be.

17 THE COURT: We know it's going to
18 be sold which is substantially all of
19 the assets.

20 MR. ZUMBRO: It's substantially
21 all of the remaining assets.

22 THE COURT: Substantially all of
23 the assets as of the petition date.

24 MR. ZUMBRO: I disagree with
25 that, sir. 60 percent is not

1 PROCEEDINGS

2 substantially all. 425 over 687 --

3 THE COURT: Those are closing
4 stores. In terms of your client's
5 brand, I mean seems to me -- well you
6 tell me, you were about to tell me, I
7 interrupted you. What was it that
8 you think the client wanted to have
9 this mark associated with? Do they
10 want it to be associated with the
11 operating assets of Sears or the sale
12 of the inventory and closed
13 nonoperating stores?

14 MR. ZUMBRO: It's a bigger issue
15 than just going out of business.
16 It's not the going out of business
17 sale. We think in order for this
18 Newco or new Sears to have the
19 ability to sell Craftsman branded
20 marks, branded products, they need to
21 enter into a new license agreement
22 with Stanley.

23 THE COURT: I know what you're
24 trying to say. What is it you're
25 protecting here? I guess if you're

1 PROCEEDINGS

2 -- I could understand why you want to
3 have consent in connection with the
4 sale of part of the brand, in
5 essence, to someone and part to
6 someone else and part to someone
7 else. But I could also understand
8 why the parties would agree that if
9 it's basically going to one entity,
10 then it's the same thing. And what
11 you're saying is that the sales that
12 are not to anybody who is using the
13 mark but just liquidation sales, I'm
14 not sure why that affects the mark
15 and why that wouldn't be consistent
16 with the parties bargain to say that
17 substantially all the assets are sold
18 then the mark can be assigned.

19 MR. ZUMBRO: Well, your Honor, I
20 think fundamentally we're trying to
21 protect the quality of the mark and
22 the brand. Your Honor, there's been
23 a lot of testimony over the last
24 couple of days about whether or not
25 Newco is or isn't a viable entity.

1 PROCEEDINGS

2 THE COURT: That's a separate
3 issue.

4 MR. ZUMBRO: But it's not, your
5 Honor, because the ability, the
6 viability of Newco to continue to use
7 our mark and potentially degrade our
8 mark is very important to us and the
9 law doesn't impose that risk on the
10 owner of a trademark license.

11 THE COURT: Unless the parties
12 agree. And I'm trying to understand
13 the basis for the agreement, I guess.
14 Again I understand your point which
15 is that there have been sales of
16 assets of the company during the
17 first couple of months of the
18 bankruptcy case. But they certainly
19 weren't operating or going concern
20 sales or sales that involved your
21 mark at all. So it's not like --
22 anyway, I understand your point. I
23 don't think you need to tell me more.
24 You succinctly stated it and clearly.
25 I'll just hear the debtor on it.

1 PROCEEDINGS

2 MR. SCHROCK: Your Honor, Ray
3 Schrock, Weil Gotshal, for the
4 debtors. Your Honor, I think you
5 have it. If you look at the record
6 in this proceeding, first of all
7 there was no cross taken, even though
8 the opportunity was there, if they
9 wanted to build a record around
10 whether or not there was some kind of
11 plan for an extended liquidation
12 either prepetition or postpetition.
13 But the agreement says that if
14 there's a transfer of all or
15 substantially all of the assets it's
16 a permitted assignment. Clearly
17 that's exactly what's happening here.
18 I don't think the testimony can be
19 read any other way from, you know, as
20 supported by any party.

21 When we enter bankruptcy we had
22 687 stores including those stores
23 that were going out of -- had GOBs
24 that were being conducted. We had to
25 shut down some stores that were

1 PROCEEDINGS

2 unprofitable. But this has been one
3 plan to try and save Sears. And
4 although we're conducting this under
5 an asset sale under 363, there's
6 nothing in this agreement first of
7 all that says substantially all of
8 the assets as were held at the time
9 of this agreement. That is not in
10 the license agreement.

11 THE COURT: That's kind of a
12 strawman. The point is that there
13 may be some creeping sale process.

14 MR. SCHROCK: And I understand
15 Mr. Zumbro pointing to cases where
16 there's several different sales and
17 it's the last step in a protracted
18 liquidation process. That's not what
19 we have here. There's been one sale.
20 And clearly the parties were
21 bargaining for this mark staying with
22 Sears. I mean that's what's
23 happening. These are the Sears
24 stores. I mean these are the Sears
25 marks. And, you know, to try and

1 PROCEEDINGS

2 take Craftsman away from the buyer
3 takes away the fundamental right that
4 we really bargained for as the
5 licensee of the mark.

6 So, your Honor, we don't think
7 there's any support under the law.
8 We think that there's no support in
9 the record and we don't think that
10 Mr. Zumbro has even built an
11 evidentiary record to support his
12 position around an extended
13 liquidation or a multipart
14 liquidation which this would be the
15 last step, and we'd ask you to
16 overrule the objection.

17 THE COURT: Okay.

18 MR. ZUMBRO: Just to respond,
19 your Honor, I think it's quite clear
20 that this company has been in sort of
21 effectively a slow moving liquidation
22 for quite some time.

23 THE COURT: Well I don't know how
24 that's quite clear. I don't really
25 have a record on that. I do have a

1 PROCEEDINGS

2 record of what's happened in the
3 bankruptcy case. But they have
4 consistently said they're pursuing a
5 going concern sale of the whole
6 business.

7 MR. ZUMBRO: I understand but --

8 THE COURT: Isn't it the same
9 headquarters, the same people running
10 it?

11 MR. ZUMBRO: A going concern sale
12 -- to be clear, we are not objecting
13 to the sale. But a going concern
14 sale --

15 THE COURT: I know you're not.
16 What I'm saying is when you look at a
17 sale of all or substantially all,
18 it's --

19 MR. ZUMBRO: I guess I wish I had
20 this in the record but Sears made
21 public statements, Eddie Lampert on
22 July 7, 2017 said going forward we
23 have a plan to start selling stores
24 and selling our unprofitable stores
25 and then only maintaining the

1 PROCEEDINGS

2 profitable stores. I think that's a
3 plan. And that is what has happened
4 since then.

5 THE COURT: It is. He's got to
6 get to -- he's got to sell it to
7 himself, right?

8 MR. ZUMBRO: He is selling it to
9 himself. We understand that and
10 that's why it's a little awkward. We
11 are using, we have the right to
12 consent to hold and bargained for the
13 right and we have a right to who
14 holds and exploit our mark.

15 THE COURT: I'm going to disagree
16 on that. I'm going to deny the
17 objection. The cure I think is just
18 reserved; is that right? I thought
19 the all cure objections were
20 reserved.

21 MR. SINGH: That's correct, your
22 Honor.

23 MR. ZUMBRO: That's fine I didn't
24 object. Just to be clear for the
25 record, they have designated the cure

1 PROCEEDINGS

2 as relating to this IP agreement and
3 it doesn't, it relates to a different
4 agreement. I just want to make sure
5 the debtors and I are on the same
6 page. I suspect you're going to deny
7 this too, I'm not asking for a stay
8 of the sale closing but I am asking
9 you orally to move for a stay of the
10 court's order that this license can
11 be assigned at tomorrow's closing.
12 I'd like a stay of that pending
13 appeal so we can pursue our appellate
14 rights.

15 THE COURT: Well --

16 MR. ZUMBRO: Because otherwise
17 it's part of the transferred assets
18 as I understand it which will be
19 assigned to the Newco tomorrow and I
20 don't want to get caught up in 363
21 (M) and statutory mootness. I'd like
22 to move for a stay pending appeal of
23 the assignment of this particular
24 agreement and their ability to use
25 the Craftsman mark pending our

PROCEEDINGS

appeal.

MR. SCHROCK: Not surprisingly,
your Honor, we object.

THE COURT: I mean it's in all
the stores, right.

MR. SCHROCK: It's used in all
the stores, there's no bond being
posted. I frankly don't think that
ESL can speak to this. I doubt the
sale is going to be going through if
we're not able to use the Craftsman
mark.

THE COURT: That means putting a
sign on every Craftsman and Black &
Decker. I think your prejudice is
outweighed here.

MR. ZUMBRO: Understood. Thank
you for your consideration, your
Honor.

THE COURT: Is that the line
going out the door there?

MS. LIEBERMAN: Hopefully not
going out the door, your Honor. Good
afternoon, your Honor, Donna

1 PROCEEDINGS

2 Lieberman from Halperin Battaglia
3 Benzija. Your Honor, we represent
4 relator Carl Ireland, administrator
5 of the estate of James Garb. The
6 objection that we filed is at docket
7 number 1931 and it's a fairly
8 discreet objection, your Honor.

9 Although as you can imagine it's one
10 that's very important to our client.

11 Your Honor, the objector as well
12 as the United States of America hold
13 a mortgage against one piece of Sears
14 real estate. That piece of real
15 estate is identified by the debtors
16 as 8975. It is listed on APA
17 schedule 1.1 P. The operating owned
18 property. So it is presumably a
19 piece of real estate that the debtors
20 wish to convey to the buyer.

21 The objection is very simple, your
22 Honor. The mortgagees have a
23 performed first lien mortgage on this
24 property. The court may recall that
25 we actually filed a limited objection

1 PROCEEDINGS

2 to the DIP motions in connection with
3 this. My colleague Mr. Halperin
4 argued that, and both the final
5 orders have specific language about
6 the fact that this mortgage is not
7 primed, nobody is pari passu with
8 this mortgage lien.

9 Your Honor, the face amount of the
10 mortgage note is \$17.4 million.

11 There is a provision in the mortgage
12 note and related documents for a
13 small amount of annual interest as
14 well as a provision for professional
15 fees. I'm sure the court will not be
16 surprised as we state in our
17 objection we do not consent to the
18 sale of our collateral. We want to
19 know that if this mortgage is not
20 going to be paid at closing, that the
21 amount of the mortgage which we
22 calculated and we've given the debtor
23 the precise number, that that amount
24 is segregated and reserved.

25 And obviously the second piece is

1 PROCEEDINGS

2 if we cannot reach agreement with the
3 debtor about the value of the
4 collateral that either party can
5 bring that issue to this court on
6 motion.

7 THE COURT: So what is the
8 debtors' proposed treatment of this?
9 I mean obviously there is protection
10 of interest in the property.

11 MR. SINGH: Sunny Singh, Weil
12 Gotshal on behalf of the debtors,
13 your Honor. I think we've got a very
14 narrow issue here. The valuation
15 reservation of rights I think we have
16 no problem with that. I think if we
17 have to come back later to deal with
18 that we can. Our position simply is
19 that under 363 (F) their liens get to
20 attach to the proceeds of sale which
21 right here as your Honor knows the
22 transaction is primarily assumptions
23 of liabilities which are the proceeds
24 that are coming in. There's no other
25 liens on this asset. So whatever

1 PROCEEDINGS

2 those proceeds may be we'll have to
3 fight about another day with the
4 objecting party but there's no basis
5 to -- they haven't traced. There's
6 no basis to say we set aside 19.8
7 million of cash that's sitting aside
8 in the company's --

9 THE COURT: I think you need to
10 give them that protection lien on
11 assets then. I don't know how they
12 are protected otherwise.

13 MR. SINGH: I believe under the
14 DIP order -- your Honor, so long as
15 it's not against a particular asset.

16 THE COURT: They have super
17 priority where they are actually
18 covered, then I think that's -- you
19 can litigate what the actual value
20 was and what you're entitled to be
21 paid.

22 MR. SINGH: Your Honor, I think
23 we would be fine with that because
24 that doesn't require any segregation
25 of whatever funds are asserted. We

1 PROCEEDINGS

2 have no problem with that.

3 MR. LIEBERMAN: Your Honor, as
4 you can imagine our only concern once
5 the value is set we know the money is
6 there and available to our client.
7 We have been hearing a great deal
8 about competing claims and whether
9 there is an administratively solvent
10 estate.

11 THE COURT: I vaguely remember
12 the carveout in the DIP order. This
13 is a first lien on this property.
14 It's worth what it's worth and it
15 can't be paid just by just saying
16 we're going to pay you some day. We
17 need to have the equivalent.

18 MR. SINGH: Your Honor, I think
19 we can add a short paragraph that
20 gives the adequate protection lien
21 that your Honor outlined with
22 everybody's rights reserved as to the
23 underlying claim.

24 THE COURT: As to the value and
25 the right to bring that issue to the

PROCEEDINGS

court.

MR. SINGH: Exactly. Thank you,
your Honor.

MR. FONG: Good afternoon, Chris
Fong from Nixon Peabody on behalf of
U.S. Bank in its capacity as the KCD
indenture trustee. We don't have any
objection to the sale. I just rise
with respect to a discrete issue that
we have with the sale documents with
which we would like to reserve our
rights. I think as you know U.S.
Bank is the indenture trustee under
indenture with KCD IP, a nondebtor
subsidiary. We've negotiated with
the debtor for the inclusion of what
is now paragraph 10 of the order
which number one reserves our rights
as indenture trustee and requires
that all the closing transactions
that are relevant to KCD be
consistent with the indenture.

Paragraph B of the order requires
that as part of closing, KCD enter

1 PROCEEDINGS

2 into exclusive licensing permit with
3 the buyer. We have not seen that
4 agreement yet. So I rise just to
5 reserve our rights to ensure that
6 that transaction complies with the
7 indenture and that nothing in the
8 order, if it is further modified --

9 THE COURT: Changes what's
10 already there. Sounds reasonable to
11 me. Any issue the debtors have with
12 that?

13 MR. SINGH: No, your Honor.

14 THE COURT: Very well.

15 MR. CICERO: Gerard Cicero from
16 Brown Rudnick on behalf of Primark.
17 Primark leases two properties from
18 the debtors. Primark is a clothing
19 retailer.

20 THE COURT: Is a tenant?

21 MR. FONG: It's a tenant in the
22 property. One of the properties it
23 leases is in Pennsylvania where the
24 debtors own that property in fee and
25 Primark just leases it. And one

1 PROCEEDINGS

2 property is in Braintree,
3 Massachusetts. The debtors actually
4 lease that from a ground lessor and
5 sublease it to Primark where Primark
6 operates its stores.

7 I rise to let you know we have
8 reached a temporary resolution of our
9 objection with the buyers. But I
10 wanted to give you a little insight
11 into what's going on. The first
12 version and the initial versions of
13 the sale orders would have sold the
14 debtors' interests in their fee
15 property and arguably in their
16 interest in property in the property
17 of the ground lease, they have a
18 ground lease to, free and clear of
19 our tenancy, of our leases, and we
20 had raised an objection under a
21 number of grounds, 365 (H) that the
22 debtors can meet 363 (F) and in the
23 alternative that under 363 (E) we
24 would request adequate protection of
25 tenancy.

1 PROCEEDINGS

2 I would say that the buyers
3 counsel and the debtors have been
4 very helpful and our issue has been
5 punted to another day should they
6 continue to want to try and sell the
7 property free and clear of our leases
8 because there has been an inclusion
9 as far as I understand it in
10 paragraph 19 of the sale order that
11 carves out tenants who have objected
12 on these bases to the free and clear
13 sale of their interest in property.

14 THE COURT: Okay. And your
15 client is one of those that's listed
16 -- not listed, anyone who has
17 objected on that basis.

18 MR. FONG: Yes. Unless your
19 Honor has any --

20 THE COURT: No, I think that's
21 reasonable resolution. I mean it may
22 be that the two leases are dealt with
23 differently under the law. I don't
24 know. It may depend. But I
25 understand your objection. I also

1 PROCEEDINGS

2 understand that you're reserving your
3 rights and therefore 363 (F)
4 objection has actually been waived --
5 not been waived, excuse me, whereas
6 those who might well beyond you was
7 waived.

8 MR. ROSENZWEIG: Your Honor, good
9 afternoon, David Rosenzweig, Norton
10 Rose Fulbright. I'm jumping in now
11 because we have the same issue.

12 THE COURT: Same issue. Did you
13 file objection?

14 MR. ROSENZWEIG: We did. We
15 represent Living Spaces Furniture
16 which is a furniture retailer that
17 has three stores, two in Arizona, one
18 in California. They sublease from
19 Sears or K-Mart the entirety of the
20 store. And we filed our objection as
21 well, raising all of those issues,
22 365 (H), 363 (F), adequate
23 protection, (E), and so we have
24 worked with ESL's counsel to include
25 in paragraph 19 the reservations for

1 PROCEEDINGS

2 those parties that filed objection.

3 THE COURT: Okay.

4 MR. SARACHEK: Good afternoon,
5 your Honor. Joe Sarachek. We filed
6 on behalf of Mein and six other
7 vendors. First of all, I want to say
8 thank you to Mr. Lampert for stepping
9 up and to the court, to Weil Gotshal
10 and the professionals who have worked
11 on this. I represent trade vendors
12 who really need Sears to stay in
13 business. They want Sears to stay in
14 business. These, you know, you
15 talked about 45,000 employees. But
16 with 10,000 vendors, there are
17 thousands, there are probably
18 hundreds of thousands of families of
19 vendors who are dependent on Sears to
20 stay in business. That said, we're
21 totally supportive of the sale. The
22 issue is timing of payment. And I've
23 been before you before to talk about
24 the 503. You asked the creditors'
25 committee attorney had he thought of

1 PROCEEDINGS

2 any ideas. Quite frankly this is an
3 unusual situation and we are
4 suggesting that the court appoint a
5 503(b)(9) ombudsman, an independent
6 party to make sure that there is 120
7 day period by which ESL is supposed
8 to pay.

9 THE COURT: They have a lot of
10 incentive here to get a plan done
11 very fast. They just want to set up
12 a litigation trust basically. But I
13 understand. I'm sorry to interrupt
14 you.

15 MR. SARACHEK: No, your Honor.
16 So it's a suggestion just so you
17 know. I'd like to take credit for
18 it, but there are a lot of far more
19 brilliant bankruptcy lawyers out
20 there.

21 THE COURT: Can I interrupt you.
22 First of all, it's M-E-M-E?

23 MR. SARACHEK: M-I-E-N. And by
24 the way, they are the nicest people.

25 THE COURT: My reaction to that

PROCEEDINGS

is the following: It seems to me that with -- if I were to approve the sale, the likelihood of these claims getting resolved promptly goes way up because there's actually someone to negotiate with then who is a customer of the vendor. I think that if the debtors and ESL don't work out a process promptly to deal with 503(b)(9) claims then someone should ask for a case conference to just literally deal with that issue. But before doing that, before adding another layer of administrative expense to the estate through another professional, I would like to see the -- now that -- well if in fact I approve the transaction, now that there will be a customer on the other side to deal with the vendor, I think those things move a lot faster in that context. If it doesn't, and by that I mean like in another few weeks, two or three weeks, you know,

1 PROCEEDINGS

2 that sort of thing, then I think I
3 might have to actually direct a
4 process, which may involve an
5 administrative layer expense or may
6 just say look you've got to do this
7 now, you've got to have a process to
8 deal with these claims now that will
9 involve the vendor and the buyer as
10 well as the debtors.

11 MR. SARACHEK: Thank you, your
12 Honor.

13 THE COURT: A lot of these are
14 small businesses.

15 MR. SARACHEK: They are.

16 THE COURT: And they're facing
17 their own financial troubles, I get
18 that.

19 MR. SARACHEK: And the issue of
20 course is that definition of receipt.

21 THE COURT: So there are two
22 things. There's a legal process
23 issue, there's a business process
24 issue. What's been lacking so far, I
25 think, is the business process

1 PROCEEDINGS

2 because you didn't know whether this
3 was going to go to liquidation or
4 sale. If it goes for liquidation
5 then that should happen right away, I
6 understand the process of liquidating
7 this claim should happen right away.

8 If it goes to the sale, then I
9 would like to give the debtors and
10 the buyer two or three weeks to come
11 up with a process that will work so
12 that they can be communicating with
13 the vendors directly in resolving
14 those issues. If that doesn't happen
15 then someone like yourself could put
16 it on the calendar so we can go over
17 it.

18 MR. SARACHEK: Thank you. One
19 other point I want to make about the
20 160 million and I'm not sure I fully
21 appreciate the issue, but if the
22 issue is what I think it is which is
23 current accounts payable, I want to
24 say to everyone, these vendors need
25 to be paid and they need to be paid

1 PROCEEDINGS

2 timely because they are out of a lot
3 of money. They're recognizing or
4 realizing their unsecured claims are
5 likely worthless and other than their
6 503(b)(9) and they need to be paid
7 and this is a big, big issue. I mean
8 this is an issue that China will hear
9 about in minutes after this hearing.
10 Thank you, your Honor.

11 MR. HONEYWELL: Good afternoon,
12 your Honor, Robert Honeywell, K&L
13 Gates for Amazon.Com Services. Very
14 briefly we are one of the parties
15 that cares about the language in
16 paragraph 19. There are some
17 procedures for reserving recoupment
18 and sell off rights. We've worked on
19 new language to the 4 a.m. order that
20 will fix that. We are reserving our
21 rights. It's a minor glitch. We've
22 worked it out with the debtors
23 attorneys and ESL.

24 THE COURT: It is not in the red
25 line I got.

1 PROCEEDINGS

2 MR. HONEYWELL: It is not in the
3 red line. It is a two word glitch.
4 We've worked it out and are
5 preserving our rights.

6 THE COURT: Is that right from
7 the debtors' point of view?

8 MR. SINGH: Yes, your Honor.

9 THE COURT: Okay.

10 MR. CHAFETZ: Eric Chafetz of
11 Lowenstein Sandler on behalf of 2, LG
12 Electronics and Valvoline LLC. I
13 rise for the same reason as Mr.
14 Gates. We've been negotiating that
15 paragraph 19 language as well and we
16 saw what we think is the final
17 version. Thank you, your Honor.

18 MR. SINGH: Your Honor, before
19 anybody else gets up I promise we
20 will fix that language.

21 THE COURT: Very well. For those
22 of you on the phone that want to be
23 heard, no one is coming up to the
24 podium so this is your time.

25 MS. COLON: Sonia Colon on behalf

1 PROCEEDINGS

2 of Santa Rosa Mall LLC. Since the
3 objections under docket --

4 THE COURT: I'm sorry, can I get
5 the name? The name of your client
6 again, it went by very quickly.

7 MS. COLON: Sonia Colon on behalf
8 of Santa Rosa Mall LLC.

9 THE COURT: Santa Rosa Mall LLC.
10 Very well, yes, ma'am.

11 MS. COLON: We have objections
12 under docket 2013 and docket 2425
13 that were filed to protect and to
14 preserve its rights to insurance
15 process for a store that was
16 destroyed as a result of hurricane
17 Irma and Maria in 2017. It was --
18 although Santa Rosa does not object
19 to the proposed after sale principal,
20 it does object and reserve its right
21 with regards to the proposed
22 retention of \$13 million inheriting
23 related insurance related process
24 when Santa Rosa is a loss payee under
25 the insurance policy for store 1915,

1 PROCEEDINGS

2 and still its motion to compel debtor
3 to the insurance process under docket
4 1240 its result in February '14.

5 Further, Santa Rosa reserves its
6 right to the transfer of any
7 hurricane insurance proceeds that may
8 have been disbursed under the
9 proposed agreement.

10 Note that under the APA, acquired
11 assets include any and all insurance
12 assets with respect to a loss or
13 damage to any acquired assets of
14 hearing prior to the asset purchase
15 agreement.

16 Despite debtors' objection last
17 Friday under docket 2013 at pages 96
18 and 97, that the \$13 million were
19 unrelated to any insurance coverage
20 under a lease agreement, the sworn
21 statements filed that day by Sunny
22 Singh under docket 2344 and
23 transferred under 2341 shows that \$13
24 million were in fact hurricane
25 insurance proceeds.

1 PROCEEDINGS

2 THE COURT: So if I can
3 understand, I'm sorry, ma'am, so let
4 me make sure I understand. You're
5 reserving your rights, there's a
6 hearing scheduled for Valentine's Day
7 I guess on the merits of this issue.
8 Or at least partly. And I guess the
9 debtors are reserving their rights.
10 You can't sell what isn't yours.

11 MR. SINGH: Your Honor --

12 THE COURT: If it is yours, the
13 debtors can sell.

14 MS. COLON: Your Honor, they
15 agree to we reserve our rights with
16 respect to the insurance process
17 that were received by the debtors or
18 any third party for the damages by
19 Hurricane Irma and Maria, but also
20 that may be received by purchasers
21 because under the acquired assets
22 that can be insurance process.

23 THE COURT: But again --

24 MS. COLON: So we need to
25 preserve the rights. We proposed

1 PROCEEDINGS

2 language that should be included in
3 the proposed order to the debtors but
4 they did not include the same in the
5 proposed orders, the redlines that
6 have been submitted to this court.

7 So we need, your Honor, that
8 reservations be included in sections
9 3 regarding the objections, and also
10 free and clear of any claims because
11 claims should be limited, that any
12 claims shall be limited to loss or
13 damages for those caused by Hurricane
14 Irma and Maria.

15 THE COURT: I think it's a
16 different concept. The free and
17 clear point goes to claims or
18 interests in assets the debtors own.
19 But the debtors don't own the asset.
20 If it's not property of the estate,
21 if it's actually someone else's, then
22 they can't sell it. I'm fine with a
23 reservation like that.

24 MR. SINGH: That's right, your
25 Honor.

1 PROCEEDINGS

2 MS. COLON: We request, your
3 Honor, in the reservation language be
4 specifically included in the order.
5 But the debtors have refused to
6 include it in the red line.

7 MR. SINGH: Your Honor, Sunny
8 Singh. If I can just respond very
9 quick. There's a reference to \$13
10 million of insurance proceeds that
11 are not being sold to which the
12 claimant -- that is coming back to
13 the estate to which the claimant is
14 asserting claims. Their rights are
15 reserved. Our rights are reserved.
16 We can be heard on the 14th. There
17 was a lot of back and forth on the
18 language to the order and frankly,
19 your Honor, what counsel laid out I'm
20 happy that their rights are reserved
21 and would stipulate that that is all
22 fine and we will deal with it on the
23 14th. These are not proceeds that
24 are actually being transferred. The
25 \$13 million reference in the APA is

1 PROCEEDINGS

2 actually a reference to being
3 retained by the estate. So it's not
4 going anywhere.

5 THE COURT: I think counsel is
6 worried -- let me finish, ma'am,
7 please. I think you were worried
8 about in the future proceeds might be
9 transferred, future proceeds that
10 might come in. And I don't know
11 whether those are proceeds the debtor
12 can sell or not, but to the extent
13 the debtor can't sell them.

14 MR. SINGH: Then they are not
15 subject to 363 (F) and we can't
16 transfer.

17 THE COURT: I don't think we need
18 to put in the order because it's a
19 given that you can't sell assets that
20 you don't own.

21 You're not making a representation
22 to ESL that you can sell assets that
23 you don't own, right?

24 MR. SINGH: No, of course not,
25 your Honor.

1 PROCEEDINGS

2 THE COURT: I think your point is
3 noted on the record, ma'am, and I
4 think it's clear.

5 MS. SONGONUGA: Good afternoon,
6 your Honor, Natasha Songonuga of
7 Gibbons, PC on behalf of the American
8 Lebanese Syrian Association, Inc.

9 This is not-the-profit section
10 501(c)(3) corporation founded
11 exclusively to raise funds for St.
12 Jude's Children Research Hospital,
13 your Honor. St. Jude's does not have
14 and does not object to the sale
15 motion as a matter of fact, your
16 Honor, I want it to be clear that St.
17 Jude's consider K-Mart which is the
18 debtor that the relationship exists
19 with to be part of the St. Jude's
20 family and together both St. Jude's
21 and K-Mart have made a tremendous
22 impact on the mission of St. Jude's
23 which is finding cures and saving
24 children.

25 I filed a limited objection on

1 PROCEEDINGS

2 behalf of St. Jude's at docket number
3 1947, your Honor, and without going
4 into the specific of that objection I
5 was advised yesterday by email that
6 either debtors' counsel or ESL's
7 counsel would be making a
8 representation to the court regarding
9 that limited objection. So far I
10 have not heard that representation
11 made to the court. I'm waiting for
12 the representation.

13 THE COURT: Now is the time.

14 MR. SINGH: Your Honor, Sunny
15 Singh, Weil, on behalf of the
16 debtors. The debtors and the buyer
17 will work with St. Jude to review and
18 work toward reconciliation of the
19 amount of funds to be turned over to
20 St. Jude on March 1 pursuant to the
21 applicable contract and the parties'
22 rights are preserved and will not be
23 prejudiced by the sale transaction.

24 THE COURT: Is that what you're
25 looking for?

1 PROCEEDINGS

2 MS. SONGONUGA: Your Honor, that
3 addresses one part. To be clear, the
4 debtors continue to collect
5 donations. There's actually
6 currently a Valentine's donation
7 campaign ongoing in the stores and
8 the debtors continue to collect
9 donation on behalf of St. Jude's.
10 Those donations are not due on March
11 1st, they're not part of the proceeds
12 that are due on March 1st.

13 THE COURT: They're not being
14 sold. Again, it's the same point.
15 It's even worse here. You can't sell
16 what you don't own. You certainly
17 can't sell what people have decided
18 to give to St. Jude's.

19 MS. SONGONUGA: Exactly. We
20 agree with that, your Honor. It was
21 not a matter of selling those
22 donations. It was just simply a
23 matter of ensuring that the purchaser
24 would be continuing to collect those
25 donation on behalf of St. Jude's.

1 PROCEEDINGS

2 MR. SINGH: Your Honor, we will
3 work with St. Jude's to deal with the
4 reconciliation and the buyers agree
5 to do that as well.

6 THE COURT: Not just --

7 MR. SINGH: Not limited to March
8 1. Whatever the amounts are.

9 THE COURT: Okay. Okay. I
10 think that I can assume then that the
11 other objections are either as was
12 previously stated being adjourned,
13 and that's largely the cure
14 objection, or been resolved or the
15 parties are reserving as to a
16 mechanism to resolve it.

17 MR. SINGH: Yes, your Honor,
18 that's exactly right. And we've got,
19 we built in most of that language,
20 I'd say 99 percent of it in the order
21 that was filed last night. We've
22 gotten some cleanup changes
23 throughout the day today that we can
24 build in. I don't think it's even
25 worth reviewing on the record some of

1 PROCEEDINGS

2 the stuff counsel have already
3 notified your Honor about. We've
4 also worked out the clarification on
5 the Cyrus release language that your
6 Honor mentioned earlier in the
7 hearing.

8 THE COURT: Okay. It's late in
9 the day, much longer than I thought
10 you have on this. But I'm happy to
11 hear very brief response by those who
12 are seeking approval of the
13 transaction.

14 MR. BASTA: Your Honor, Paul
15 Basta from Paul, Weiss from the
16 subcommittee. I literally have one
17 minute. Mr. Qureshi pointed out my
18 testimony from the podium, all the
19 numbers in my argument tie to Mr.
20 Carr's declaration. Your Honor --

21 THE COURT: Well in bankruptcy
22 cases there are times when the
23 lawyers who are speaking to you who
24 are intimately involved in the very
25 things that they're being asked

1 PROCEEDINGS

2 about, such as a meeting takes place,
3 etc., so I take those representations
4 by people who are subject to
5 discipline from me as close to
6 evidence.

7 MR. BASTA: Understand, your
8 Honor. Your Honor had a discussion
9 with Mr. Qureshi about what it meant
10 to give up equitable subordination
11 because as a remedy it would mean
12 that the debtors would then have to
13 go and chase a recovery. A primary
14 defendant in the debtors' litigation
15 claims that is not included in the
16 complaint that's attached to the
17 standing motion that the committee
18 filed is of course Seritage. And if
19 your Honor looks on Yahoo, you'll see
20 that Seritage has a market cap of
21 \$2.27 billion and ESL's interest --

22 THE COURT: That actually is
23 evidence. But I understand the
24 point.

25 MR. BASTA: I'm just saying I

PROCEEDINGS

know that is evidence. I'm just saying ESL owns 45 percent of Seritage. So when we looked at it from the collection issue, ESL had a significant interest in Seritage which has a large market cap and Seritage itself is a significant defendant. The third point, your Honor, Mr. Qureshi pointed out the letter from ESL attacking the subcommittee somehow tainted the process. I think the record is uncontroverted that Mr. Carr and Mr. Transier made their decisions without any fear and without any bias and in fact rejected the ESL bids after the receipt of that letter.

MR. SCHROCK: Your Honor, Ray Schrock, Weil Gotshal, for the debtors. Subject to any questions you have actually, I'm willing to stand on the record before you.

THE COURT: Actually I did have a couple of questions I forgot to ask

1 PROCEEDINGS

2 you when you were speaking this
3 morning. I have the statement by the
4 consumer privacy ombudsman in which
5 she makes a number of
6 recommendations. She says as long as
7 the debtors and ESL abide by those
8 recommendations she supports the
9 sale. She thinks it's proper as far
10 as the bankruptcy code and the
11 applicable law with regard to
12 consumer identifying information and
13 other related topics.

14 So I have the debtors and ESL
15 agreed to those recommendations?

16 MR. SCHROCK: Yes we have, your
17 Honor.

18 THE COURT: And ELS to?

19 MR. SCHROCK: Yes, your Honor.

20 THE COURT: All right. And then
21 my other issue here is what is your
22 response on the argument that Mr.
23 Qureshi made that certain of the
24 assets being purchased here aren't
25 being purchased with the noncredit

1 PROCEEDINGS

2 bid portion of the sale?

3 MR. SCHROCK: Your Honor, I just
4 don't think that's frankly consistent
5 with the asset purchase agreement,
6 that assertion, as well as the record
7 in this case.

8 They are -- ESL is purchasing,
9 with the credit bid and then they are
10 paying off senior secured claims.
11 And by the way, we keep calling them
12 the unencumbered assets. The DIP
13 loans have liens on those assets as
14 course. The DIP loans have to be
15 repaid.

16 THE COURT: The DIP loans have
17 liens on Dove and Sparrow?

18 MR. SCHROCK: Certainly I believe
19 on the equity, the underlying equity
20 that the debtors hold, that's
21 correct, your Honor.

22 THE COURT: And anything else?

23 MR. SCHROCK: Yes. And so
24 there's, you know, as your Honor
25 noted there's 3.9 billion.

1 PROCEEDINGS

2 THE COURT: It's like 850 million
3 of DIP loan?

4 MR. SCHROCK: That's correct,
5 there's 850 million of DIP loan,
6 there's \$350 million Junior DIP
7 that's there.

8 THE COURT: I'm sorry to
9 interrupt you. The committee's
10 argument is that there's 560 million
11 of equity value in Dove and Sparrow
12 and 233 in IPGL so that's less than
13 the DIP loan.

14 MR. SCHROCK: Your Honor, we will
15 rely on the record as to the value of
16 the collateral but we didn't get
17 there on the map. It was a
18 presentation.

19 THE COURT: Assuming that value.

20 MR. SCHROCK: Yes.

21 THE COURT: Okay. Mr. Qureshi,
22 any response on that?

23 MR. QURESHI: Your Honor, I'm not
24 sure that that's consistent with how
25 the DIP order is supposed to work and

1 PROCEEDINGS

2 in particular the mash lane
3 provisions under the DIP order.

4 THE COURT: I thought they waived
5 marshalling. I mean they normally
6 do.

7 MR. QURESHI: Your Honor, again,
8 I don't think that's how --

9 THE COURT: Can I interrupt you.
10 I know there were reservations of
11 rights with respect to the Junior
12 DIP. But on the senior DIP I thought
13 there was a waiver of 506 (C) and
14 marshalling.

15 MR. QURESHI: Your Honor, let Mr.
16 Dublin handle that question.

17 THE COURT: Okay, he's the
18 financing guy.

19 MR. DUBLIN: Phil Dublin, Akin
20 Gump. I don't have the DIP order
21 handy, your Honor. But when we
22 negotiated the DIP, the final DIP
23 order with the ABL lenders we
24 actually had a whole construct of
25 marshaling built in where there was

PROCEEDINGS

marshaling waiver except there's a provision in the back of the order which I don't remember the paragraph number that provides that even in connection with a sale process, the proceeds of the sale are supposed to be used, that are applicable to what was prepetition ABL collateral, I think that might be the defined term, are used in a specific order distribution, such that, for example, here, since the new ABL loan is being funded and the collateral for the new ABL loan is are the ABL assets that exist at the company, the proceeds from that new ABL loan that come into the estate should be used to repay the existing ABL DIP, thereafter whatever prepetition ABL obligations have not been repaid which I think what's left is the FILO and the LC facility which have liens on the ABL assets and then after that there's a whole litany of order of marshaling.

1 PROCEEDINGS

2 That's also included in the Junior
3 DIP order. I apologize, I don't have
4 the document with me. But I believe
5 that that's the way the marshaling
6 provisions work, notwithstanding the
7 fact that technically there's a
8 marshaling waiver.

9 MR. SCHROCK: But again, your
10 Honor, we don't have the luxury of
11 evaluating this bid in a vacuum.
12 Indisputably, there's billions of
13 dollars of assumed liabilities that
14 are general unsecured claims,
15 administrative claims that are being
16 put into and are being paid off.

17 THE COURT: I understand that
18 point. If you look at it in the
19 aggregate, I understand.

20 MR. SCHROCK: Right.

21 THE COURT: Dove and Sparrow are
22 separate debtors? Or are they --

23 MR. SCHROCK: The Sparrow
24 entities are in a REMIC structure,
25 where we hold the equity. They're

PROCEEDINGS

not debtors.

The court: Right. So I mean --

MR. SCHROCK: But that equity is held by the debtors.

THE COURT: I'm assuming, because I thought they were like special purpose real estate entities, that they don't have a lot of the types of debts that ESL is taking on.

So you have to look at other value that's going to them which would be the DIP and there's some carveout.

MR. SCHROCK: Right, your Honor. But I think when I just look at the -- when you think about the -- in a winddown, right, there's going to be a number --

THE COURT: All I'm saying is I just want to make sure that the sale is fair to those particular debtors. Now the easiest way to make sure of that is to see whether they are obligated in respect of debts that are being repaid one way or the other

1 PROCEEDINGS

2 including with cash taking out the
3 DIP.

4 MR. SCHROCK: But we've been
5 servicing their collateral with money
6 that's being generated from sales.
7 It's an integrated operation.

8 THE COURT: The other way to
9 ensure that it's fair is to recognize
10 some sort of intercompany claim
11 against the people who get the
12 benefit.

13 MR. SCHROCK: And those are all
14 reserved.

15 THE COURT: I would like to look
16 at the DIP order which I had printed
17 out actually last night. So I think
18 I can find it pretty quickly. All
19 right. Anyone else? Okay. I'm
20 sorry, Mr. Bromley, I have a question
21 of you.

22 MR. BROMLEY: That's why I sat
23 over here, your Honor.

24 THE COURT: This issue about the
25 \$166 million, your favorite issue. I

1 PROCEEDINGS

2 have the schedule now. There's no
3 dispute that that was the schedule
4 that was attached to the agreement,
5 correct?

6 MR. BROMLEY: Correct.

7 THE COURT: And I have the
8 provisions in the agreement that
9 relate to this issue. There are
10 assumption provision and the cross
11 reference to the definitional
12 provision of other payables.

13 So I understand the debtors'
14 argument completely on this one.
15 What is the -- in terms of the plain
16 language of the agreement, what is
17 ESL arguing?

18 MR. BROMLEY: Can I get the
19 document, your Honor?

20 THE COURT: Sure.

21 MR. BROMLEY: So, your Honor, do
22 you have the document in front of
23 you?

24 THE COURT: Do the debtors have
25 the most recent version of the APA?

1 PROCEEDINGS

2 MR. SINGH: Your Honor, there's
3 been no change to the original
4 version. But we do have copies.

5 THE COURT: So the amendments
6 don't cover this.

7 MR. SINGH: The amendment does
8 not relate to this issue. But we
9 have extra copies.

10 THE COURT: Can you give me an
11 extra copy.

12 MR. SINGH: Yes. Just a moment,
13 your Honor.

14 MR. SCHROCK: We have to find the
15 box.

16 MR. SINGH: Yes, just the
17 transition over.

18 THE COURT: You can just read it.

19 MR. SINGH: Your Honor, it is
20 quoted in the presentation.

21 MR. BROMLEY: Do you have the
22 debtors' presentation from earlier?

23 THE COURT: Yes, the slides from
24 today?

25 MR. SCHROCK: It's slide 24, your

1 PROCEEDINGS

2 Honor. That's the relevant language
3 that's quoted here.

4 THE COURT: Right. Okay.

5 MR. BROMLEY: Your Honor, the way
6 that the document works is section 2
7 of the asset purchase agreement,
8 article 2, deals with purchase and
9 sale, with section 2.1 being the
10 purchase and sale of the acquired
11 assets. And section 2.2 dealing with
12 the excluded assets.

13 Section 2.3 deals with the
14 assumption of liabilities. So this
15 is the way a standard asset purchase
16 agreement is structured. So what
17 you're buying, what you're not buying
18 and then what you're assuming.

19 So section 2.3 is the assumption
20 of liabilities and the header for
21 that says on the closing date the
22 buyer shall assume effective as the
23 closing and timely perform and
24 discharge in accordance with their
25 respective terms the following

1 PROCEEDINGS

2 liabilities.

3 If you go to 2.3 K, there are
4 several things that are going on in
5 2.3 K and it has a total of 10
6 subsections.

7 So what 2.3 K says that the
8 assumed liabilities include the
9 severance reimbursement obligations,
10 which is a defined term. The assumed
11 503(b)(9) liabilities, other
12 payables, defined term, and all
13 payment obligations with respect to
14 the ordered inventory.

15 And then there's the 10
16 subsections which a couple of them
17 reference these terms.

18 But then when you go back to the
19 definitions, so you have other
20 payables as a defined term and
21 ordered inventory is a defined term.

22 MR. SCHROCK: Your Honor, those
23 are on the next page, the next slide,
24 ordered inventory as well as the
25 other schedule.

1 PROCEEDINGS

2 MR. BROMLEY: So when you look at
3 other payables, and that is on page
4 24, other payables shall mean the
5 accounts payable set forth on
6 schedule 1.1 G. Ordered inventory,
7 another defined term, shall mean
8 inventory, which itself is a defined
9 term, other than prepaid inventory.
10 Again, a defined term. Of the type
11 set forth on schedule 1.1 F that has
12 been ordered by the sellers prior to
13 the closing date but as to which the
14 sellers have not taken title or
15 delivery prior to the closing date.

16 So if you go back to 2.3 K and
17 look at the -- and each of those have
18 a schedule. So if you go to schedule
19 1.1 F which is ordered inventory, and
20 I'm not sure if that's in your chart.

21 MR. SCHROCK: It is.

22 MR. BROMLEY: That's on page 23
23 of the slide deck you got this
24 morning, your Honor.

25 THE COURT: 25.

1 PROCEEDINGS

2 MR. BROMLEY: I'm sorry, 25, yes.

3 And that box at the bottom is exactly

4 how it appears and how I've cut it

5 out and put it in the back of my

6 binder. And so what does it say? It

7 says ordered inventory. Ordered

8 inventory, and then it says as of

9 January 7, 2019. And it has two

10 categories, domestic and imports. It

11 has a total line. Total on order,

12 less paid in transit, less on the

13 order, total amount of ordered

14 inventory. And you go all the way

15 over to the far right-hand side, 278

16 million total on order, deducting

17 what has been paid in transit and is

18 on the order which is also in effect

19 title is transferred, you get total

20 of 166,557,000. But there are two

21 things that are important to keep in

22 mind about the way schedule 1.1 F is

23 written and how ordered inventory is

24 defined. Ordered inventory on

25 schedule 1.1 F is ordered inventory

1 PROCEEDINGS

2 as of January 7, 2019. So this is an
3 example, your Honor, this is not a
4 definition, this is going to be the
5 ordered inventory as of the moment of
6 closing.

7 Because if you go back to what the
8 definition of closing is it says
9 goods of the type set forth on
10 schedule 1.1. So it's not saying
11 it's exactly on 1.1, meaning 1.1 F as
12 an example. That has been ordered by
13 the sellers prior to the closing
14 date, as to which the sellers have
15 not taken title or delivery prior to
16 the closing date.

17 So what we have is anything as to
18 which there are orders out but it
19 hasn't been delivered, title hasn't
20 been taken.

21 That's what ordered inventory
22 means.

23 It just so happens that as of
24 January 7, 2019 schedule 1.1 had a
25 number of \$166.6 million.

1 PROCEEDINGS

2 That is what from ESL's
3 perspective in terms of the
4 negotiations it was having with
5 respect to the bid letter that it put
6 in dated January 5th, because that's
7 when this was added in, the
8 expectation for ESL was that what we
9 were doing with respect to the
10 accounts payable was that we were
11 taking accounts payable that relate
12 to ordered inventory, that is
13 accounts that are -- amounts that are
14 going to be due for inventory that
15 was paid that has not yet been
16 received but will be delivered after
17 the closing date. And so that number
18 is \$166 -- as of January 7th was
19 \$166.6 million.

20 And it was that number that we
21 were operating in respect of.

22 Now other payables is defined term
23 as well. And if you go to 2.3 K it
24 says other payables is the accounts
25 payable set forth on schedule 1.1 G.

1 PROCEEDINGS

2 And that schedule was made public
3 today. And that schedule simply is
4 an amount that says \$166 million.
5 That is on page 24 of the deck from
6 this morning.

7 So there's no -- schedule 1.1 G is
8 not a schedule of particular
9 payables, it's a dollar amount,
10 right.

11 And so if you go further down in
12 2.3 K, and there's sub numbers,
13 romanettes i through l, there is
14 romanette v, buyers' obligation with
15 respect to the other payables shall
16 not exceed \$166 million in the
17 aggregate.

18 It's not a coincidence that the
19 number \$166 million is with respect
20 to both the schedule relating to
21 ordered inventory or other payables
22 because it was indeed the parties'
23 intention, at least is ESL's point of
24 view, that what other payables meant
25 in 2.3 K is that it's other payables

1 PROCEEDINGS

2 and payment obligations with respect
3 to the ordered inventory.

4 So that total amount is \$166
5 million. The schedule 1.1 F makes it
6 clear that the ordered inventory
7 expectation was \$166 million.

8 THE COURT: But if it was other
9 payables and all payment obligations
10 and you define other payables in 5,
11 little roman v you say buyers'
12 obligation with respect to the other
13 payables and all payment obligations
14 shall not exceed \$166 million. This
15 just refers to the other payables,
16 not the clause that follows it and
17 all payment obligations with respect
18 to ordered inventory.

19 MR. BROMLEY: I hear what you're
20 saying, your Honor. But there's no
21 other use of the word ordered
22 inventory. What we're talking about
23 here it may be that ordered inventory
24 is an additional defined term that's
25 not necessary. The but what we're

PROCEEDINGS

talking about --

THE COURT: The parties defined it.

MR. BROMLEY: But it's the exact same definition. It's \$166 million. It's the same number, your Honor.

MR. SCHROCK: But that's why we had two schedules.

THE COURT: Why are you fighting over it? If it's the same thing then it's 166 either way.

MR. BROMLEY: The point is whether there's two 166s or one, the schedule that Mr. Schrock refers to is not a schedule, it's just a number on a page. That's not a schedule.

THE COURT: But it is because that's what the schedule says.

MR. SCHROCK: Right. But, your Honor, the other payables are payables that exist, right, that we specifically negotiated as a bridge out of insolvency.

THE COURT: I don't care what

PROCEEDINGS

people negotiated. It looks to me the parties used two different terms, they define them differently and put a cap on one and assumed the other one. Now it may be that definitionally they overlap in which case there's no reason to pay more than once but if they don't overlap --

MR. BROMLEY: Your Honor I think at a minimum there's an ambiguity here and there are no documents in the record because it's not the time to do it.

THE COURT: I'm not deciding this issue today because I can't but I don't see ambiguity. You can't make one under New York law by saying the parties disagree about what they meant unless the document itself is ambiguous.

MR. BROMLEY: I understand, your Honor.

THE COURT: Hang on just for a

1 PROCEEDINGS

2 second. Is Mr. Dublin here still?

3 MR. DUBLIN: Yes.

4 THE COURT: Can you just look and
5 see where this provision is.

6 MR. SINGH: Your Honor, I think
7 it's paragraph 13.

8 MR. SCHROCK: Paragraph 13 for
9 the senior DIP.

10 THE COURT: What page is that, do
11 you know?

12 MR. SINGH: It starts on page 37
13 if you have the senior DIP order,
14 your Honor.

15 THE COURT: Yes, I do.

16 MR. SINGH: It's a very, very
17 longer paragraph.

18 THE COURT: Sorry.

19 MR. BROMLEY: That's okay.

20 THE COURT: I don't really need
21 -- I now understand the rationale.

22 MR. BROMLEY: But I have some
23 more.

24 THE COURT: Okay. Go ahead. No,
25 go ahead.

1 PROCEEDINGS

2 MR. BROMLEY: I'm sorry, your
3 Honor. The fact is that that's not
4 the only point. There's two -- that
5 these two definitions are sitting
6 here together is not happenstance.
7 But what we are talking about as well
8 is that there is an ongoing
9 obligation of the debtors with
10 respect to these numbers to be
11 performing the base, to operate the
12 business in the ordinary course. To
13 order things and pay for them as they
14 come due, right. And what we know --

15 THE COURT: That's a separate
16 issue. Debtors haven't looked for a
17 different interpretation of that.

18 MR. BROMLEY: It is and it isn't,
19 your Honor. To the extent what has
20 happened is to the extent there's two
21 buckets which we don't agree with and
22 this one bucket is being filled up
23 because what is happening is the
24 debtors are not paying their
25 obligations as they come due, they

1 PROCEEDINGS

2 are violating another portion of the
3 agreement. This is an
4 extraordinarily complex document.
5 But it cannot be on the one hand the
6 debtors can choose voluntarily not to
7 pay things.

8 THE COURT: The debtors are
9 willing to live with the ordinary
10 course provision, right?

11 MR. SCHROCK: We are, your Honor.

12 MR. BROMLEY: Your Honor to the
13 extent there's a dispute going
14 forward I want to let you know the
15 issues are to whether or not the
16 debtors are performing --

17 THE COURT: I understand that
18 point. Correct me if I'm wrong, but
19 I think the concern that the special
20 committee and the debtors had was
21 that, was not over that issue, but
22 rather over the first argument you
23 made.

24 MR. SCHROCK: That's correct,
25 your Honor.

1 PROCEEDINGS

2 MR. BROMLEY: I know because
3 they're not concerned about the first
4 issue because it helps them because
5 what they've been doing is not
6 performing in the ordinary course.

7 THE COURT: The ordinary course
8 is a separate provision.

9 MR. BROMLEY: They relate to each
10 other, your Honor.

11 THE COURT: Well, I don't know.
12 Okay. Thank you.

13 MR. BROMLEY: Thank you, your
14 Honor.

15 THE COURT: Page 37 you said, Mr.
16 Singh?

17 MR. SINGH: One second, your
18 Honor.

19 THE COURT: This is a five-page
20 paragraph. I have what's called the
21 final order.

22 MR. SINGH: It's paragraph 13,
23 page 37 where we start talking about
24 reverse marshaling provisions. As
25 you say, your Honor, it's a very long

1 PROCEEDINGS

2 paragraph. If you go to page 40,
3 right after the definition of reverse
4 marshaling provisions, your Honor. I
5 think the relevant provision we were
6 talking about before is that the DIP
7 ABL agent shall not apply proceeds of
8 prepetition unencumbered.

9 THE COURT: Received in
10 connection with any exercise of
11 secured credit or remedies or any
12 sale, transfer, such asset.

13 MR. SINGH: That's right, your
14 Honor. So the point of the provision
15 being that the senior DIP ABL agents
16 agree to personal space on the
17 inventory and then if they came up
18 short they would look to the other
19 unencumbered collateral. But it
20 wasn't that they didn't have a lien
21 on the other unencumbered collateral,
22 your Honor.

23 THE COURT: I don't think Mr.
24 Dublin was saying they don't have a
25 lien, it's just a marshaling

1 PROCEEDINGS

2 provision. I think he summarized
3 that correctly. Amazing he
4 remembered all of that. All right.

5 So I have before me a motion by
6 the debtors in these cases for
7 approval of an asset purchase
8 agreement as modified, and related
9 exhibits and documents, between them,
10 to create an entity that is going to
11 be owned by the debtors controlling
12 shareholder ESL and other parties who
13 will be in a minority position in
14 that Newco.

15 The Second Circuit has been
16 addressing motions for the approval
17 of the sale of all or substantially
18 all of the business of a debtor in
19 possession which this sale in essence
20 is. For decades, starting with in re
21 Lionel Corp, 722 Fed 2nd 1063, Second
22 Circuit, 1983, in which the Second
23 Circuit held that a debtor in
24 possession can sell all or
25 substantially all of its assets

1 PROCEEDINGS

2 outside of a Chapter 11 plan,
3 provided that the judge finds a good
4 business reason based on the evidence
5 before him or her. That's at page
6 1071.

7 And the sale is not outside of a
8 plan is not the result of undue
9 pressure separate and apart from
10 there being a good business reason.

11 The sale here at this point is
12 essentially unopposed, with the
13 exception of an objection by the
14 debtors official creditors'
15 committee.

16 I have dealt with the other
17 objections which are primarily
18 reservations of rights with the
19 exception of the Craftsman, Black &
20 Decker objection which I dealt with
21 on the merits, but that involved the
22 assignment of one particular asset, a
23 trademark license.

24 The creditors' committee does not
25 oppose the sale of substantially all

1 PROCEEDINGS

2 of the assets outside of a Chapter 11
3 plan. Indeed, the basis, the primary
4 basis for its objection is that it
5 would rather have all the assets sold
6 on a liquidation basis outside of the
7 -- outside of the Chapter 11 plan.

8 So the standard by which I should
9 review the sale here is the essential
10 standard laid out by Lionel which
11 again is the court needs to find a
12 good business reason based on the
13 evidence before it as that standard
14 has evolved over the years.

15 It's important to note at the
16 outset the Second Circuit has made it
17 clear that these types of motion,
18 even though they are of extreme
19 importance in a bankruptcy case, are
20 summary proceedings. That is, the
21 court, unless the proceeding is
22 combined with an adversary
23 proceeding, is not to determine
24 interest in property or other issues
25 that might affect the sale on a final

PROCEEDINGS

basis, but rather, needs to determine the merits of the proposed sale itself.

See, for example, in re Orion Pictures 4 F3 1095 Second Circuit 1993 and in re Genco Shipping and Trading Limited, 509, 445, Bankruptcy SDNY 2014.

The general inquiry that the court should make when considering the propriety of a sale motion under section 363 (B) of the bankruptcy code is well laid out by Judge Lane in re Advanced Contracting Solutions LLC, 582 B.R. 285 through 10, bankruptcy SDNY 2011, quote, section 363 (B) of the bankruptcy code governs the proposed sale or use of estate property outside the ordinary course of business. The standard for approval under section 363 (B) of whether the debtor exercised sound business judgment.

The case law concerning section

PROCEEDINGS

363 provides that the court needs to review the business decision and whether it was made on a disinterested basis with due care and good faith and according to some courts, truncated, there's no abuse of discretion and waste of corporate assets.

See also in re GMC 407 B.R. 463, 294 bankruptcy SDNY 2009 where the court held to approve a section 363 (B) sale the court must be satisfied that notice had been given to all creditors and interested parties, sale contemplates a fair and reasonable price that the purchaser is proceeding in good faith.

A number of courts in this district, with the seminal case being in re Resources Inc. 47 B.R. 650 at 656 SDNY 1992, and including the Advanced Contracting case that I quoted, go further and say that in analyzing whether the proposed sale

PROCEEDINGS

is a proper exercise of good or sound business judgment, the court may apply the business judgment rule which essentially as determined by courts is a rule applying to transactions in nonbankruptcy context that presumes that court and decisionmakers and the decisions, presumes, excuse me, the corporate decisionmakers and the decisions will be protected from judicial second guessing. And that courts are loath to interfere with corporate decisions absent issuing a case of bad faith, self interest or gross negligence and will uphold the board decisions as long as they are attributable to any rational business purpose, with the burden being on parties opposed to the exercise of such a decision.

And I appreciate the analysis that the courts in this district have done to apply that standard. But I have consistently held and believe that

1 PROCEEDINGS

2 Lionel and Orion and the plain
3 language of the statute require more
4 inquiry at least where the
5 substantive objections to the
6 proposed sale which is the case here.

7 Ultimately as laid out by the
8 Second Circuit in the Orion Pictures
9 case, albeit that case involved a
10 business decision to assume or reject
11 contracts, but that decision was
12 still done in the ordinary course.
13 And I think the logic therefore
14 applies to section 363 (B),
15 ultimately the decision as laid out
16 by the Second Circuit in Orion
17 Pictures is one where the bankruptcy
18 court has to exercise its business
19 judgment to determine in light of all
20 of the facts laid out on the record
21 in a summary proceeding whether in
22 fact the decision does make business
23 sense to sell the assets as proposed
24 by the debtor.

25 And that's the standard that I've

1 PROCEEDINGS

2 applied here. The Second Circuit in
3 putting that burden on the bankruptcy
4 court also made it clear that the
5 bankruptcy judge is looking into the
6 future and therefore cannot assure
7 the benefits of the proposed
8 transaction, but nevertheless needs
9 to evaluate it based on what it knows
10 in the present day to decide whether
11 in fact the transaction makes good
12 business sense.

13 In doing so, the courts are guided
14 by not only the underlying
15 consideration being provided for the
16 assets but also the process by which
17 the assets were sold and whether it
18 was generally fair and within the
19 constraints under which the selling
20 party was operating in some
21 circumstances and the like designed
22 to maximize the value.

23 The case law is clear that section
24 363 (B) sales does not require a
25 formal auction process as is

1 PROCEEDINGS

2 confirmed by the SDNY guidelines on
3 asset sales developed by the judges
4 in the bankruptcy court in the
5 Southern District, and that with the
6 right process, sales to insiders may
7 be approved.

8 However, an inquiry into the
9 process is clearly warranted,
10 especially where the sale is to an
11 insider as is the case here.

12 Again, though, the Second Circuit
13 has given the bankruptcy courts
14 guidance in dealing with sale
15 processes. As stated by the Second
16 Circuit in re Financial News Network
17 Inc., 980 if 2nd 165 and 166, Second
18 Circuit 1992, bankruptcy court must
19 perform a difficult balancing act
20 when it conducts an auction of the
21 debtors' assets. It walks a
22 tightrope between on the one hand
23 providing for an orderly bidding
24 process recognizing the danger of the
25 absence such a fixed bidding process,

1 PROCEEDINGS

2 bidders may decline to participate in
3 the auction, while on the other hand,
4 retaining the liberty to respond to
5 different circumstances so as to
6 obtain greatest return for the
7 bankrupt estate.

8 What one takes away from that
9 opinion and subsequent opinions is
10 that as reflected in the sale
11 procedures order entered by the court
12 to govern the process for selling the
13 debtors' assets, regular procedures
14 are important so that parties can
15 rely on them, but overall supervision
16 by the court with the input from key
17 parties in interest including the
18 debtors in the exercise of their
19 fiduciary duties, the creditors'
20 committee and other interested
21 parties, is necessary to deal with
22 issues that come up during the sale
23 process and that need to be addressed
24 if in fact addressing them will lead
25 to increased value in a fair manner.

1 PROCEEDINGS

2 The last couple of points I will
3 make generally on court's standard
4 for reviewing this motion is that
5 typically courts will consider
6 whether the sale price was fair and
7 the transaction in which its being
8 paid is one that makes good business
9 sense, by looking to the sale price
10 for all of the assets together,
11 without discussion of the constituent
12 parts.

13 And as a subset of that
14 proposition, the courts recognize
15 that provided that one keeps within
16 the priorities in the bankruptcy
17 code, there may be individual
18 constituencies in a case who benefit
19 more from a sale than others. For
20 example, those who are parties to
21 executory contracts or unexpired
22 leases whose contracts are being
23 assumed by the buyer will have their
24 prepetition claims cured or there
25 will be adequate assurance of a cure.

1 PROCEEDINGS

2 Whereas other unsecured creditors,
3 after the payment of the sale
4 proceeds to senior creditors may get
5 far less in respect of their
6 unsecured claims.

7 Nevertheless, such a sale, as long
8 as the overall price is fair, and
9 again it doesn't violate other
10 provisions of the bankruptcy code,
11 will be approved.

12 See, for example, in re TWA, 2001
13 Bankruptcy, Lexis 980, Delaware,
14 April 2, 2001 in re 100 US, 674, 677,
15 Bankruptcy SDNY 1989. See also
16 Mission Iowa Wind Company V Enron
17 Corp 291 B.R. 39, 43 SDNY 2003.

18 That case, that is the Enron
19 Mission Wind case however also stands
20 for another proposition which is
21 that, as I said before, its sale
22 cannot violate substantive rights
23 except as permitted by the bankruptcy
24 code, for example, under section 363
25 (F) of the court -- of the code or

1 PROCEEDINGS

2 violate the general priority scheme
3 of the bankruptcy code.

4 So, for example, in the Mission
5 Wind case the debtor sought approval
6 of a sale of assets that included not
7 only its own assets but assets of
8 nondebtor entities.

9 Obviously the proceeds of that
10 sale need to be allocated among the
11 two sellers which the district court
12 required to be done on a thorough
13 basis.

14 It is also important if assets are
15 being sold by more than one debtor to
16 ensure that no particular debtor is
17 shortchanged for the assets that it
18 is selling in respect of the sale
19 proceeds or consideration received
20 from the sale so that to the extent
21 that it has separate creditors, those
22 creditors are not prejudiced.

23 There has been a fair amount of
24 talk during the trial in the summary
25 proceeding as to whether or not the

1 PROCEEDINGS

2 proposed sale would leave the debtors
3 after the sale administratively
4 insolvent, that is, unable to pay
5 their postpetition and 503(b)(9)
6 prepetition administrative expenses
7 in full as is required under a
8 Chapter 11 plan for that plan to be
9 confirmed, unless the administrative
10 expense creditors waive that right.

11 There is no requirement under the
12 bankruptcy code to ensure that a
13 proposed sale of substantially all of
14 the assets that have been operating
15 the business result in administrative
16 solvency.

17 Indeed, the opinions a number of
18 opinions recited in the debtors'
19 memorandum of law to the contrary but
20 even more so there are hundreds of
21 cases that are resolved in going
22 concern sales with the subsequent
23 dismissal of the case, with unpaid
24 administrative expenses.

25 The court's concern about

1 PROCEEDINGS

2 administrative solvency nevertheless
3 is real because the debtor needs to
4 be left with resources to ensure that
5 the transaction's benefits will be
6 received and generally speaking one
7 wants to get as many claims paid as
8 possible. But it is in that context
9 that I reviewed the testimony
10 regarding the fact of the proposed
11 sale on the administrative solvency
12 of these debtors.

13 This sale motion has resulted in a
14 far longer evidentiary hearing than
15 most sale motions. I heard the
16 testimony of ten witnesses live as
17 well as reviewed deposition
18 designations of one other witness,
19 Mr. Kniffen, and deposition
20 designations from Mr. Diaz, one of
21 the committee's experts.

22 There are also several binders of
23 agreed exhibits which have been
24 admitted into evidence.

25 But it appears clear to me, having

1 PROCEEDINGS

2 heard all of that testimony and
3 reviewed the evidence as deemed to be
4 significant by the parties that
5 essentially there are three
6 underlying grounds for the creditors'
7 committees objection to the proposed
8 sale.

9 The first is that the sale process
10 under which the debtors proceeded
11 with the marketing of their assets
12 that resulted in the sale that's
13 sought to be approved today was
14 flawed to such an extent that the
15 sale should not be approved, or if it
16 were to be approved, I should not
17 provide a finding under section 363
18 (M) of the bankruptcy code that the
19 purchaser engaged in transaction in
20 good faith, which is essentially the
21 same thing as saying that I would not
22 approve the sale because no purchaser
23 would enter into an agreement without
24 that.

25 The second argument that the

1 PROCEEDINGS

2 committee has made is that in light
3 of the only reasonable alternative
4 here, which is a prompt liquidation
5 of the debtors' assets, the proposed
6 going concern sale is deficient,
7 i.e., the hypothetical liquidation of
8 the debtors' assets would result in a
9 higher or better transaction.

10 Finally, the committee has argued
11 that there is insufficient value
12 being provided by purchaser here over
13 and above its credit bid in relation
14 to assets that it is purchasing that
15 are not encumbered by a lien that
16 would support the credit bid.

17 I'll address each of those
18 objections in order.

19 But before doing so, I will note
20 that currently there are no
21 objections to the proposed sale by
22 any party to executory contract or
23 lease that is sought to be assumed in
24 today's order L, other than cure
25 objections which the parties have

1 PROCEEDINGS

2 agreed to resolve in the future.

3 In other words, no party today
4 whose contract is being assumed or
5 whose lease is being governed by this
6 order, has objected today on the
7 grounds of a lack of adequate
8 assurance and future performance.

9 The parties have been careful to
10 reserve all rights in respect of that
11 issue, in respect of any lease that
12 is not specifically being assumed at
13 the closing or executory contract,
14 except where there's not been an
15 objection and no express reservation
16 of rights.

17 As I noted, I entered an order
18 approving a sale process here that
19 contemplated taking bids for all or
20 substantially all of the debtors'
21 assets as well as bids for
22 substantial portions of the debtors'
23 assets which could then be aggregated
24 if they were submitted in a
25 qualifying way to compete as a group

1 PROCEEDINGS

2 to any bid that were made for all or
3 substantially all of the assets.

4 I also made it clear that any
5 party seeking to make a proposal for
6 real estate assets should do so and
7 the debtor should take such proposals
8 seriously.

9 The record here is clear that to
10 thoroughly market the debtors' real
11 estate assets one would need a
12 minimum of four months.

13 The committee's expert has opined
14 that it would be a disaster to market
15 the real estate assets for anything
16 less than over a year and as much as
17 20 months.

18 Obviously the debtors here could
19 not therefore run a full real estate
20 marketing process along with a going
21 concern sale process that also would
22 have contemplated bids for
23 substantial portions of the debtors'
24 business to be aggregated as I stated
25 earlier.

1 PROCEEDINGS

2 Nevertheless, as I said, those
3 wishing to make material bids for
4 real estate were encouraged strongly
5 to put their best foot forward by me
6 to do so in the bidding procedures
7 order contemplated.

8 The bidding procedures order also
9 contemplated that the creditors'
10 committee, and other parties in
11 interest, would have the right to
12 come back to this court and to
13 complain about how the process was
14 being conducted in real time and to
15 seek a prompt pivot if the process
16 was not being conducted in a way that
17 would maximize value to a liquidation
18 process that would start the active
19 marketing of the debtors' real estate
20 assets in a manner that I previously
21 described.

22 I have reviewed the testimony here
23 on the process issues, including from
24 the debtors's side the testimony by
25 Brandon Aebersold and the two

PROCEEDINGS

independent directors, William Transier and Alan Carr. I've also considered the testimony of the committee's investment banker Saul Burian, and I conclude that as far as a going concern sale process is concerned, the debtors engaged in a thorough and fair process given the constraints under which they were operating, namely, the need that all parties recognize, including the creditors' committee, that they could not sustain continuing operations for any meaningful length of time.

The committee through Mr. Burian has complained that certain potential buyers of segments of the debtors business were confused or given short shrift during the sale process and that that is a reason there were only indicative, or insufficient, rather, expressions for bids for parts of the debtors that might be hiked off on a standalone basis.

1 PROCEEDINGS

2 I have considered that allegation
3 carefully and conclude that given the
4 nature of this process as supervised
5 by me on a hands-on basis, that all
6 parties in interest, including Mr.
7 Burian, knew if indeed these problems
8 were truly troublesome, they would
9 have been raised to me so that I
10 could have stepped in to have ensured
11 either a little more time or a little
12 more focus to maximize potential
13 competing offers. None of that
14 happened.

15 It is also reasonably clear to me
16 based on the testimony not only by
17 the debtors's directors that I
18 previously mentioned but certainly
19 other witnesses that the so-called
20 potentially standalone businesses are
21 closely integrated with the rest of
22 Sears and that there are meaningful
23 issues related to separating them
24 that would potentially adversely
25 affect a potential buyer's

1 PROCEEDINGS

2 willingness to bid for such assets.

3 That's I believe simply a fact
4 that may well go to explain why the
5 bidding for those assets was not more
6 robust.

7 The committee has also complained
8 as a process matter that the insider
9 purchaser tainted the sale process to
10 its advantage. As a set of facts to
11 support that conclusion, committee
12 has pointed to three or four things.

13 Before addressing them, I should
14 note that the debtors then controlled
15 by ESL and before the commencement of
16 these cases, and with ESL's consent,
17 replaced ESL as the controlling party
18 for purposes of a transaction of this
19 kind as well as review of any claims
20 against ESL independently and as how
21 that may relate to a transaction of
22 this kind, to third parties, the
23 restructuring committee and then a
24 subset of that restructuring
25 subcommittee. Those independent

1 PROCEEDINGS

2 third parties were represented by
3 independent counsel and financial
4 advisors.

5 The two members of the
6 restructuring subcommittee testified
7 in the hearing before me on the sale
8 motion, Mr. Transier and Mr. Carr.

9 I believe the record is crystal
10 clear that the restructuring
11 committee and restructuring
12 subcommittee, A, actually had control
13 of the debtors with respect to the
14 sale process and the debtors'
15 decision throughout that process as
16 to whether to accept or reject any
17 offers and how to conduct the
18 process, B, that they were in fact
19 truly independent as evidenced by,
20 among other things, their rejection
21 of numerous proposals by ESL and
22 heated and lengthy negotiations with
23 ESL, C, that they were well and
24 thoroughly advised by independent
25 professionals, and D, that their

1 PROCEEDINGS

2 focus was a proper one, which
3 essentially is the same standard that
4 I've already outlined. Does the
5 proposed transaction represent the
6 highest or best transaction available
7 to these debtors?

8 I believe that they exercised
9 their responsibilities in an active
10 and informed way and that they
11 themselves were experienced in this
12 area and brought their experience to
13 bear, as opposed to being passive
14 receptacles for their profession's
15 advice. There are numerous incidences
16 in the record to reflect that.

17 Under the circumstances,
18 therefore, I believe that the
19 involvement of the proposed buyer
20 here as a bidder for the assets was
21 effectively neutralized in respect of
22 the debtors' review of that bid and
23 the process that led to the bid and
24 the bid's acceptance.

25 The committee, that is the

PROCEEDINGS

creditors' committee has attacked that process I believe only by pointing to the fact that after Mr. Transier first met Mr. Lampert, the controlling party of ESL, that meeting having been by phone, to lay out the -- at a board meeting that laid out the duties of the new board members of the restructuring subcommittee and the fact that a joint office of the CEO would be formed, including Mr. Meghji and Mr. Riecker and Mr. Transier, and therefore Mr. Lampert stepped down from making any decisions over the fate of Sears.

Mr. Transier sent an email to Mr. Lampert in which he stated to Mr. Lampert that he admired how Mr. Lampert had handled those sensitive issues. Given the sensitivity of that transfer, I believe the email was appropriate. I don't believe it indicated that Mr. Transier took any

1 PROCEEDINGS

2 less seriously his role as an
3 independent director, co-CEO and
4 member of the restructuring
5 subcommittee. Rather, it was simple
6 diplomacy dealing with someone who
7 potentially would regret and
8 therefore cause problems later the
9 decision that he had made to turn
10 over power over the fate of what had
11 been his company to people he had
12 never met before.

13 There was no suggestion of any
14 subsequent communications between Mr.
15 Transier and Mr. Lampert that would
16 indicate Mr. Transier was anything
17 other than an independent director
18 who recognized that the company's
19 interests separate and apart from Mr.
20 Lampert and ESL needed to be
21 protected and that it was his job to
22 do so.

23 The committee also points to a
24 letter sent by, among others, Mr.
25 Riecker, one of three of Sears senior

1 PROCEEDINGS

2 managers, to the board stating that
3 they strongly hoped that the board
4 would seriously consider a going
5 concern exit for Sears as opposed to
6 a liquidation.

7 There is evidence in the record
8 that Mr. Riecker and the other
9 authors of that letter were
10 approached by Mr. Lampert before they
11 sent the letter and that they ran the
12 letter by Mr. Lampert's counsel.

13 But having assessed Mr. Riecker's
14 credibility on the witness stand, it
15 is clear to me that that letter and
16 the sentiment behind it came from him
17 personally and that he would have
18 sent it whether Mr. Lampert told him
19 to or not.

20 Finally, the committee challenges
21 the process not based on how the
22 parties who were charge of the
23 process conducted it or evaluated it,
24 but to the contrary, on the actions
25 of ESL in the process.

1 PROCEEDINGS

2 It points to two things. First, a
3 letter sent on behalf of ELS to the
4 debtors' board during the course of
5 negotiations leading up to the
6 January 15th sliding into the end of
7 January 16th period auction.

8 The letter was sent at a time when
9 the restructuring committee and
10 restructuring subcommittee quite
11 firmly indicated to ESL that it was
12 not going to accept the current
13 proposal by ESL that was then on the
14 table and was instead prepared to
15 pivot to a liquidation.

16 The letter threatened the board
17 with legal action for abuse of
18 fiduciary -- brief of fiduciary duty
19 if it so took -- if it took such an
20 action.

21 The debtors' counsel, the
22 restructuring committee and
23 restructuring subcommittee's counsel,
24 committee's counsel and other parties
25 raised this issue immediately with

1 PROCEEDINGS

2 the court which held a chambers
3 conference on the issue and which
4 those parties as well as ESL's
5 counsel participated.

6 I made it clear in no uncertain
7 terms that that letter was a mistake
8 and should be ignored by all parties,
9 including those who were handling the
10 sale on behalf of the debtor,
11 including the independent board
12 members.

13 It is clear both from the letter
14 and I made it clear at the chambers
15 conference that the letter did not
16 recognize that one of the major
17 reasons, if not the only reason that
18 ESL's proposals had been rejected is
19 that ESL was still insisting on a
20 global release of all claims against
21 it. In other words, the letter was
22 half-baked.

23 I believe that it had literally no
24 effect on the subsequent negotiations
25 other than perhaps giving the

PROCEEDINGS

negotiators on behalf of the company
a little more negotiating leverage
against ESL, because obviously I
wasn't happy with the letter had been
sent and had so characterized it. But
clearly it did not give ESL any more
negotiating leverage or affect the
sale price.

When I weigh that one mistake
against the actions that ESL took to
enable this sale process to be
conducted in an independent way, it
is clear to me that all told, ESL
conducted itself in this case with
respect to the sale process in good
faith for the purposes of 363 (M) of
the bankruptcy code.

The committee has also pointed to
prepetition actions by ESL that it
contends means that it did not engage
in good faith in the sale process
that has led to the sale today.

The evidence supporting that
contention is frankly rather vague in

1 PROCEEDINGS

2 the record, but I gather the argument
3 is that some time in the past ESL
4 started to cause the sale of Sears
5 but resisted until shortly before the
6 bankruptcy petition date actually
7 setting up a structure to enable the
8 sale in a meaningful way.

9 Besides the evidentiary issue that
10 I already addressed, my focus is
11 primarily if not exclusively on the
12 postpetition period in section 363
13 (M) .

14 Moreover, I don't really
15 understand the argument in the first
16 place to have a true sale process
17 here of a store that relies on trade
18 credit and the like, one needs to act
19 fast and generally in a bankruptcy
20 environment because the sale would
21 not have happened except in a
22 bankruptcy environment.

23 So conducting the type of sale
24 process that apparently the committee
25 thinks Mr. Lampert and ESL should

1 PROCEEDINGS

2 have conducted or Sears should have
3 conducted some time before the
4 petition date, truly is not
5 realistic.

6 Certain of the groundwork could be
7 laid, but the actually process it
8 would have to go through for a
9 business of this kind, a court
10 supervised process, under the
11 bankruptcy code, because no buyer
12 really would take these assets at
13 this point, I believe without a court
14 order protecting them.

15 I believe the properties -- I'm
16 sorry. Let me back up.

17 I believe that the law is further
18 clear that my focus should be on the
19 postpetition period, not actions that
20 the buyer may have taken prepetition.
21 See in re Wingspread Corp. 92 B.R.
22 87, Bankruptcy, SDNY 88.

23 But more importantly, I don't see
24 the rationale behind the arguments
25 under the facts before me which

1 PROCEEDINGS

2 reflect again I think a more
3 important reality which is that there
4 really were no other going concern
5 buyers here and the parties
6 reasonably understood the liquidation
7 alternative and used the value that
8 could have been derived in the
9 alternative effectively in
10 negotiating with ESL.

11 So I conclude that the process
12 here was proper and appropriate. If
13 anyone wanted to, they could have
14 complained. Mr. Mahane, counsel for
15 a group of landlords, did complain at
16 one point, the day of the auction,
17 and as I said during the trial I
18 responded to him I believe within
19 five minutes as well as to debtors'
20 counsel to make it clear that the
21 landlords could attend -- continue to
22 make proposals if they wanted to.

23 But notwithstanding the various
24 protestations of an improper sale
25 process, I did not receive other

1 PROCEEDINGS

2 complaints until after the fact.

3 The second basis for the objection
4 is that the proposed transaction is
5 inferior to a liquidation sale of the
6 debtors. To be clear, this appears
7 to me to be primarily a dispute over
8 the value of the debtors' real estate
9 assets. And secondly, the likelihood
10 that ESL will perform the noncash
11 payment aspects of its proposed
12 purchase agreement.

13 It is true that the debtors have
14 -- would have in a liquidation
15 scenario the ability to sell certain
16 business segments, although I believe
17 the parties agree and frankly if they
18 didn't I believe it to be the case
19 that the value of those business
20 segments is substantially tied to an
21 ongoing Sears and would be greatly
22 reduced if Sears were liquidated.

23 I believe there's little
24 disagreement with the value of those
25 segments or frankly about the other

1 PROCEEDINGS

2 assets besides real estate that is in
3 any way meaningful.

4 The parties do disagree over the
5 realizable value of the debtors' real
6 estate. I carefully considered the
7 testimony offered on that subject by
8 Michael Welch, the debtors' expert
9 from Jones Lang LaSalle and to some
10 extent Mr. Meghji, the debtors' CRO,
11 and from the company's side -- I'm
12 sorry, from the committee side Mr.
13 Greenspan of FTI Consulting.

14 I found that the assumed value of
15 the debtors real estate to the debtor
16 as opposed to those that might have a
17 lien on that real estate, ie., those
18 who would be entitled to the proceeds
19 before they received them, to be
20 credibly set forth by Mr. Welch and
21 supported by Mr. Meghji.

22 Mr. Welch's valuation assumed the
23 reality here which is that the pivot
24 to a real estate sale would be
25 extremely difficult given a number of

1 PROCEEDINGS

2 the debtors' properties and the big
3 box size of so many of them, as well
4 as the fact that, with respect to the
5 debtors's leased assets, which
6 comprise most of the real estate
7 assets, the debtors' ability to keep
8 landlords at bay under section 365
9 would end at the beginning of May of
10 this year by which point any landlord
11 who believes that there in fact is
12 value in the lease would have a
13 strong incentive not to consent to a
14 further extension of the time to
15 assume or retract.

16 Any buyer would know that too and
17 therefore would prefer to deal with
18 the landlord directly as opposed to
19 the debtor.

20 So the debtors' window for real
21 estate sale process was constrained
22 as Mr. Welch properly opined.

23 Committee has criticized the
24 debtors' valuation of the real estate
25 other than focusing on the timing

1 PROCEEDINGS

2 point by noting that where there were
3 indicative bids for the real estate.
4 Even if those bids were substantially
5 smaller than the professional
6 estimations by Jones Lang LaSalle,
7 the debtors included them as a
8 datapoint equally with the other
9 appraisal information.

10 There is something to be said for
11 the committee's point, particularly
12 if an indicative bid was a clear
13 outlier as was the case with many of
14 the bids for certain leases or other
15 real estate assets.

16 On the other hand, given the I
17 believe relatively small number of
18 large potential bidders, the response
19 by potential bidders for the real
20 estate to the court's invitation to
21 put their best foot forward at least
22 an indicative bid was certainly
23 underwhelming.

24 I believe it's consistent, at a
25 minimum, with Mr. Welch's view that

1 PROCEEDINGS

2 given the number and size of the
3 debtors' real estate assets, the
4 parties wanted to keep their options
5 open to see how the case shook out.

6 That works both ways. They then
7 put their best bid forward but they
8 also were reserving their right to
9 make a much lower bid in the future
10 if the debtors negotiating leverage,
11 as was inevitable with the ticking of
12 the clock under section 365, would
13 decrease.

14 In any event, Mr. Meghji testified
15 that the delta if it were included as
16 the debtors did, those indicative
17 bids in the valuation and if the
18 debtors didn't include it, was
19 roughly \$70 million which no one on
20 the committee side is contradicting.

21 Mr. Greenspan in dealing with
22 another \$70 million error which he
23 recognized did not actually reflect
24 it in one of his valuations because
25 he said it was just a mere rounding

PROCEEDINGS

error.

Turning to Mr. Greenspan, I don't think I have ever seen an appraisal of a real estate portfolio that was more divorced from reality than his determination that you should value these assets based on an 18 to 22 month marketing period. That is simply not what the debtors had available to them.

When you take that out of his calculation, and when you recognize, as one must, that the period really would be approximately four months, the valuations are substantially the same.

The other minor number of assets that FTI evaluated that the debtors didn't evaluate could be potentially available to the debtors, was limited to about 20 percent according to Mr. Greenspan's testimony of the assets the debtor didn't evaluate at all.

Of that 20 percent, he appears to

1 PROCEEDINGS

2 have not recognized that in a number
3 of cases there were prior lien
4 holders that would have a right to
5 all of the proceeds, that they would
6 in fact not be paid in full for the
7 proceeds before the debtor estate
8 would. And at least in one case
9 that, by his own analysis, comprised
10 approximately 10 percent of that
11 extra value. He clearly just got
12 wrong whether the debtor was paying
13 any current rent under the lease.

14 His explanation for that omission
15 frankly didn't make sense to me. He
16 said that the market rent number of
17 \$8.50 must actually reflect the
18 arbitrage number, ignoring the fact
19 that the very next column was headed
20 arbitrage and also had the 8.50
21 number. So clearly the arbitrage was
22 the whole market rent that he stated.

23 Obviously that was just 1/10 of
24 the unencumbered asset valuation that
25 the debtors didn't undertake but it

PROCEEDINGS

certainly cast more doubt on his testimony which frankly I completely discounted anyway given his view on the ability of the debtors to conduct a real estate sales that he posits within the time frame that he posits. It's simply not a viable basis for comparison to the deal presently before the court.

That leaves the committee's argument that the value in the ESL transaction, which I find, I found it to be on its face 5.2 billion clearly exceeds the value to the estate of a liquidation approach based on the foregoing analysis.

The committee, as I said, contends that that value isn't really there, that it's illusory. I conclude to the contrary, that there's a reasonable basis to believe that in fact the value will be received by the debtors.

There are several different issues

1 PROCEEDINGS

2 that this raises, or this analysis
3 raised. First, the debtors contend
4 that the limited release that ESL
5 will receive as part of this
6 transaction leaves the debtors with
7 substantial valuable litigation
8 claims against ESL, that the release
9 is carefully confined to equitable
10 subordination and recharacterization
11 claims for which ESL is paying not
12 only \$35 million but also the
13 entirety which is premised on a
14 portion of the deal, \$1.3 billion
15 being the credit bid and settlement
16 of ESL's recovery in respect of its
17 allowed claims from other assets of
18 the estate.

19 It appears to me based on oral
20 argument at least that the committee
21 when pushed does actually recognize
22 that the release is in fact limited
23 and that the remaining causes of
24 action are appropriately preserved.

25 The committee contends, and this

1 PROCEEDINGS

2 is a tautology, that in granting the
3 release that would be granted to ESL,
4 the estate is giving up a potential
5 revenue which is to limit the
6 recovery that ESL in the bankruptcy
7 case through equitable subordination
8 or recharacterization and that come
9 constant with that the proceeds that
10 would otherwise go to ESL from
11 liquidation would go to other
12 creditors.

13 I have two responses to that
14 argument. The first is that it
15 appears to me that there are
16 substantial sources of recovery at
17 ESL and assets that it owns including
18 Seritage that remain available to the
19 estate on its litigation claims.

20 Secondly, I want to reiterate that
21 the underlying causes of action that
22 are preserved have essentially the
23 same quantum of proof as equitable
24 and subordination claims have.

25 Unfortunately for her,

1 PROCEEDINGS

2 Judge Chapman has had to deal with
3 these issues more than her fair share
4 in the recent past, including in re
5 Light Square Inc. 511 B.R. 253
6 Bankruptcy SDNY 2014 and in re Sabine
7 Oil and Gas Corp 547 B.R. 503, SDNY
8 2016.

9 In those cases she goes through
10 the elements of equitable
11 subordination and I think accurately
12 summarizes them.

13 In addition to building that it is
14 a remedial equitable power and that
15 the remedy is limited to
16 subordinating the claim to the extent
17 of being actual damages and damages
18 would need to be shown for equitable
19 claims outside of bankruptcy as well,
20 although fraudulent transfer, the
21 transfer is what would be avoided.

22 She states that courts in this
23 district have held that there is no
24 different or heightened standard by
25 which to judge a noninsider's conduct

1 PROCEEDINGS

2 for purposes of equitable
3 subordination, though there may be
4 fewer traditional grounds available
5 because neither under capitalization
6 or breach of fiduciary duty applies
7 to conduct of a noninsider, that's at
8 page 340.

9 Here the debtors are preserving
10 breach of fiduciary duty claims and
11 other equitable claims. It's a
12 complete overlap.

13 So in other words, Sears gets to
14 reorganize but these claims are
15 preserved nevertheless. To me, that
16 is a completely fair and reasonable
17 settlement considering all of the
18 issues including collection issues.

19 Secondly, the committee contends
20 that certain of the obligations that
21 ESL is undertaking to pay don't have
22 to be paid immediately upon closing,
23 but will be paid over time, albeit
24 over a relatively short period of
25 approximately three to four months at

PROCEEDINGS

most. In that context, it challenges the ESL business plan that was introduced into evidence and supported by the testimony of not only ESL's witness, Mr. Kamlani but also Mr. Meghji, Mr. Riecker and to some extent Mr. Transier and Mr. Carr, although to a much more limited extent.

That business plan in itself is premised upon a standalone business plan that Sears developed shortly after the start of these bankruptcy cases for a somewhat larger footprint of stores, 505 instead of 425.

The committee points out that in the past Sears has dramatically underperformed as against projections. The debtors have pointed out that in the more recent past, the remaining months before the bankruptcy filing which I acknowledge is a brief period, the debtors have actually or did actually perform well

1 PROCEEDINGS

2 consistent with their projection and
3 consistent with the projections in
4 the Sears and ESL business plans, or
5 at least reasonably consistent with
6 those projections, given that under
7 the ESL business plan one is talking
8 about 80 fewer stores and a far lower
9 debt load and dealing with stores
10 that truly have value.

11 I have carefully reviewed Mr.
12 Kniffen's deposition excerpts that
13 were introduced to go along with his
14 declaration which I've also carefully
15 reviewed. I do not view his
16 concededly expert testimony with any
17 greater degree of deference than the
18 testimony I received from Mr.
19 Kamlani, Mr. Riecker or the other
20 debtor witnesses. Clearly the latter
21 group are far closer to the actual
22 facts of Sears. Mr. Kniffen has not
23 actually worked in retail since 2005.
24 He's been a consultant to people who
25 are interested in retail since then.

1 PROCEEDINGS

2 But he's not actually had the
3 pleasure of dealing with the
4 admittedly, he admits this, changed
5 environment over the last decade for
6 big box retailers.

7 For the period that really is at
8 issue here, which is the next several
9 months, I believe, based on the
10 evidence before me, that ESL, or the
11 buyer will in effect -- will, in
12 fact, rather, perform its obligation
13 under the agreement.

14 If it breaches the agreement, it
15 will be the subject of every lawsuit
16 including equitable subordination and
17 it will have lost a substantial new
18 investment that it will be making in
19 this business.

20 Accordingly, I conclude that the
21 execution risk for this transaction,
22 when one considers the alternative
23 which has its own execution risk, is
24 reasonable to take.

25 One aspect of the transaction

1 PROCEEDINGS

2 creates additional execution risk
3 with respect some time on oral
4 argument. It is the proper
5 interpretation of section 2.3 (K) of
6 the asset purchase agreement as set
7 forth in the Orion Pictures case that
8 I previously cited. Given the
9 procedural context of this matter, I
10 cannot conclude that issue, those two
11 different interpretations,
12 dispositively. See also in re Sabine
13 Oil and Gas Corp 550 B.R. 59,
14 Bankruptcy SDNY 2016.

15 I do, however, have an obligation
16 to review the issue, make sure I
17 understand it and determine how I
18 believe it would turn out with a
19 proper record and a proper procedural
20 context, just as Judge Chapman did in
21 the Sabine case that I just cited
22 when she interpreted a similar
23 contract issue.

24 Based on my review of section 2.3
25 including subsection K, subsection

PROCEEDINGS

roman V of that subsection K and the schedule, that is incorporated into the definition of the defined term other payables which appears in the definitional section of the agreement, as well as my evaluation of the analysis given to me by ESL's counsel that includes a review of the defined term other inventory that appears in the APA and schedule 1.1 F that deals with other inventory, I believe it's reasonable to assume that the debtors' interpretation of 2.3 would prevail in a proper litigation, namely, that the parties defined separately the concept of other payables from all payment obligations with respect to ordered inventory, which is the clause that precedes the words other payables in section 2.3 K.

And further that the parties clearly set forth in little roman v of subsection K that the cap of 166

1 PROCEEDINGS

2 million would apply only to other
3 payables, not to the phrase that
4 follows those two words in subsection
5 K, namely, quote, and all payment
6 obligations with respect to ordered
7 inventory.

8 I'm more than reasonably confident
9 that would be the result in a
10 contested matter brought before the
11 court under the part 7 rules.

12 That leaves of course the debtors
13 with their obligation to make a
14 supplement agreement, the agreement
15 will control obviously, conduct their
16 operations in the ordinary course for
17 closing and any other rights under
18 the agreement that either party has.

19 For the debtors it seems to me
20 they are willing to live with that,
21 those terms in the agreement.

22 There are certain other conditions
23 to the agreement, closing conditions
24 that need to be satisfied. I am
25 reasonably confident, based on Mr.

1 PROCEEDINGS

2 Meghji's testimony, Mr. Riecker's
3 testimony, particularly that they
4 will be, and further, that the
5 parties will deal with each other in
6 good faith to enable those conditions
7 to happen, particularly given the
8 identification of ESL with this
9 business of the consequences that
10 would happen to it, that is, the
11 Sears business with which its
12 identified, if they do not deal with
13 each other in good faith to resolve
14 those conditions to closing.

15 The last point I will make,
16 although I believe only the asset
17 side really needs to be addressed and
18 I've already done so when comparing
19 the ESL transaction to the
20 liquidation alternative, but I will
21 nevertheless mention that in each of
22 the committee's calculations it has
23 made assumptions regarding the
24 treatment of ESL's claims in these
25 cases that I believe are not

1 PROCEEDINGS

2 warranted and that would at a minimum
3 lead to substantial litigation and
4 litigation risk for the estates,
5 namely the committee has assumed that
6 notwithstanding a pivot to a
7 liquidation sale and its request, the
8 estate would be able to prevail on
9 making substantial charges to the
10 underlying collateral that secures
11 the ESL secured debt and the DIP
12 loans.

13 The ability to surcharge
14 collateral under section 506 (C) of
15 the bankruptcy code is constrained by
16 the language of the statute itself
17 and the case law, including the
18 leading case of in re Flagstaff Food
19 Service Corporation, 739 F2d 73,
20 1984.

21 See also in re Domistyle Inc. 811
22 F 3rd 691, Fifth Circuit 2015, cert
23 denied 2017, US Lexis 2509, May 30,
24 2017.

25 Those cases make it clear that the

PROCEEDINGS

determination of surcharge and collateral is a difficult one for a court that requires the courts to make judgments as to whether the expenses incurred by a debtor were for the primary and direct benefit of the secured creditor as opposed to other parties in interest in the case. This issue is usually dealt with by stipulations between the parties because they know how difficult it is to litigate.

Properly here the committee insisted on certain carveouts from 506 (C) waivers, but that didn't eliminate the difficulty of litigating such an issue.

The word primary does not appear in the statute, but the courts have applied it because otherwise as the Domistyle court notes, the statute could in essence eat up the narrow -- the interpretation could eat up the narrow nature of the statute which is

1 PROCEEDINGS

2 a direct benefit.

3 Secondly, the committee has
4 completely discounted any right that
5 ESL would have under section 507(B)
6 to a super priority administrative
7 expense based on the decline of its
8 collateral value since the start of
9 the bankruptcy cases.

10 Until disallowed, ESL's secured
11 claim is entitled to adequate
12 protection including under 361.3, the
13 super priority claim under sections
14 503 B and 507(B).

15 Determining the decline in value
16 of the collateral during the course
17 of the bankruptcy case is again an
18 extremely difficult issue. It was
19 dealt with by Judge Glenn in re
20 Residential Capital LLC 501 B.R. 549
21 bankruptcy SDNY 2013. It's fact
22 based, dependent upon the value of
23 the collateral at time one and time
24 two. To give absolutely no
25 consideration to that claim I believe

1 PROCEEDINGS

2 in terms of comparing creditor
3 recoveries under a liquidation
4 process to the ESL going concern
5 transaction I believe is quite
6 inappropriate.

7 So for all of those reasons, I
8 will grant the motion. I believe the
9 proposed order needs some work along
10 the lines of the remarks that were
11 stated on the record and oral
12 argument today. But that that work
13 is relatively modest and would appear
14 to me that I should be in a position
15 to enter it tomorrow morning if it's
16 provided to me in black letter form.

17 That will conclude, for the
18 reasons that I stated on the record,
19 a finding that the transaction
20 entitled under section 363 (M) of the
21 bankruptcy code.

22 I would like to say one other
23 thing which is simply to echo the
24 remarks that Mr. Seltzer made not
25 only on behalf of the prospective

1 PROCEEDINGS

2 union employees but all employees for
3 this company.

4 During the course of this case Mr.
5 Lampert in particular and ESL
6 generally has been subject to
7 substantial verbal abuse. He is a
8 wealthy individual and a big boy and
9 I guess he can take it. Some of it
10 based on past years may be justified
11 or may not be justified. That will
12 be part of the record in the
13 litigation that's fully preserved
14 here.

15 I can say that that abuse has led
16 to, as Mr. Bromley kind of probably
17 more eloquently than I'm about to
18 say, summarized two conflicting views
19 of him that he's somehow Jay Gould
20 and Barney Fife at one and the same
21 time. He has the opportunity now not
22 to be a cartoon character and to take
23 actions that I believe Mr. Kamalani
24 mentioned would in fact be of great
25 meaning to the debtors constituents.

PROCEEDINGS

He should do that. A clear communication process, both with vendors but important with employees is really warranted. Okay. Thank you.

MR. SCHROCK: Thank you, your Honor.

(Matter concluded at 3:53 p.m.)

C E R T I F I C A T E

STATE OF NEW YORK)

: ss.

COUNTY OF NEW YORK)

I, MARK RICHMAN, a Certified
Shorthand Reporter, Registered Professional
Reporter and Notary Public within and for
the State of New York, do hereby certify
that the foregoing proceedings were taken
before me on February 7, 2019;

That the within transcript is a
true record of said proceedings;

That I am not connected by blood
or marriage with any of the parties herein
nor interested directly or indirectly in the
matter in controversy, nor am I in the
employ of the counsel.

IN WITNESS WHEREOF, I have
hereunto set my hand this 7th day of
February, 2019



MARK RICHMAN, C.S.R., RPR